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HOMEOWNERSHIP AFFORDABILITY

HEARING

BEFORE THE

SUBCOMMITTEE ON
HOUSING AND URBAN AFFAIRS

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDREDTH CONGRESS

FIRST SESSION

ON

THE DISTURBING EVIDENCE THAT HOMEOWNERSHIP IS BECOMING AN INCREASINGLY ELUSIVE PART OF THE AMERICAN DREAM DUE TO THE SOARING HOME PRICES AND HOW THE PROBLEM HAS AFFECTED ECONOMIC DECISIONS OF BUSINESSES AND INDIVIDUALS

JULY 1, 1987

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CONTENTS

WEDNESDAY, JULY 1, 1987

Page

Opening statement of Senator Cranston 1

Opening statements of:

  Senator Dixon 3

  Senator Sasser 4

  Senator D'Amato 4

WITNESSES

H. James Brown, director, MIT-Harvard Joint Center for Housing Studies, Cambridge, MA 5

Robert R. McMillan, Esq., chairman, Long Island Association's Committee on Housing, Uniondale, NY 39

Cathlene Wells, public school teacher, Los Angeles, CA 46

Ardath Cade, assistant secretary for housing and community development, Annapolis, MD 60

Terrence R. Duvernay, executive director, Michigan State Housing Development Authority, Lansing, MI 70

Orest T. Dubno, executive director, Connecticut Housing Finance Authority, Rocky Hill, CT 75

Mark Hendrickson, executive director, Florida Housing Finance Agency, Tallahassee, FL 88

James Fischer, president, National Association of Home Builders 103

Ira Gribin, first vice president, National Association of Realtors 121

Lyle Gramley, chief economist and senior staff vice president of the Mortgage Bankers Association of America 144

Earl Corkett, president, Mortgage Insurance Companies of America 159

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

Statement of the Council of State Housing Agencies 169

HOMEOWNERSHIP AFFORDABILITY

WEDNESDAY, JULY 1, 1987

U.S. Senate,
Committee on Banking, Housing, and Urban Affairs,
Subcommittee on Housing and Urban Affairs,
Washington, DC.

The subcommittee met at 9:35 a.m., in room SD-538 of the Dirksen Senate Office Building, Senator Alan Cranston (chairman of the subcommittee) presiding.

Present: Senators Cranston, Graham, D'Amato and Chafee.

OPENING STATEMENT OF SENATOR CRANSTON

Senator Cranston. The hearing will please come to order.

This morning's hearing considers the affordability of homeownership in the United States. We will explore why the dream of homeownership is slipping out of reach for a growing number of Americans, particularly those who are trying to buy their first home.

That dream of homeownership is a foundation stone of our society. For most Americans, it is the largest source of family wealth. It bestows a sense of independence, achievement, and family stability.

The dream of homeownership remains as powerful today as ever. It remains a strong aspiration—despite increases in real estate rates and construction costs and despite substantial changes in the size and character of families. According to survey after survey, the overwhelming majority of Americans, including young Americans, regard homeownership as their highest personal priority.

Yet there is disturbing evidence that homeownership is becoming an increasingly elusive part of the American dream. After 35 years of steady increase, homeownership rates began to decline in 1980 and have not rebounded since. The bulk of that decline has occurred among home buyers who are 25 to 34 years old.

It isn't hard to see why. To make payments on an average priced house in the 1950's, a typical 30-year-old person had to spend 14 percent of his or her paycheck. By the 1970's, the required share of income rose to 21 percent. By 1985, it hit an astounding 44 percent, more than double from 10 years earlier, more than triple from the 1950's.

As Senator from California, I know firsthand about the negative impact of high housing costs. Until very recently, home prices in major metropolitan areas of California were consistently higher than anywhere else in the country, with San Francisco and Los Angeles sharing the ranking for highest home prices for both new and existing housing.

Soaring home prices tell a sobering story. According to the National Association of Realtors, the median price of an existing single family home in 1986, was $80,300 nationwide. But in San Diego, it was $118,200. In Los Angeles, it was $128,800. In Orange County, it was $147,400. And in San Francisco, it was $164,000—that is double the nationwide level. Not surprisingly, only 31 percent of California's households, based on their income bracket, could have afforded to buy the median-priced home during 1986. That is 31 percent, in my State, compared to 47 percent for all U.S. households.

The 69 percent of California's households who have been priced out of the homeownership market includes just about everyone who is beginning their career as a public school teacher, policeman, firefighter, construction worker or factory worker. These people realize that they are increasingly unlikely ever to be able to own a home in or near the community where they work.

That is bad news for families and bad news for our cities.

High housing prices have also had negative implications for a number of local economies. In San Francisco, for example, businesses are finding it increasingly difficult to recruit needed employees. In addition, longer commutes for workers has created more traffic, more pollution, higher absenteeism and quicker employee turnover. That explains why major corporations throughout the Bay Area helped form the Bridge Housing Corp. to help close the affordable housing gap.

The problem of affordable housing is a key issue which will be addressed in next year's major housing legislation. Tomorrow in Los Angeles, the subcommittee will initiate an ambitious, year-long effort to build a national consensus around a new national housing policy.

The subcommittee has convened this hearing today to receive a more detailed picture of how severe the affordability problem is on a national level. I am grateful that an outstanding group of witnesses has agreed to join us to offer their views on the nature and size of this problem.

In specific, we have requested witnesses to address the issues of which age and income groups are most affected by this problem, where geographically the problem is most concentrated, how the problem has affected economic decisions of businesses and individuals and what aspects of the problem have not generally been recognized.

We have also asked the witnesses to consider how the Federal Government might ease the difficulties faced by first-time home buyers. As this subcommittee moves forward with its agenda of producing a major piece of housing legislation in the coming year, the observations and recommendations of today's witnesses will be invaluable.

So I welcome you all here today. I look forward to hearing your testimony.

I want to say the following to our witnesses. I ask each of you to please summarize your full statement in 5 minutes. Your full written statement will be included in the record. We will also keep the record open for 2 weeks for you to respond to any additional questions that a Senator might have.

Any additional questions will be sent to you within 1 week of this hearing, and we hope you can respond within 1 week.

Our first panel will present us with an overview of the problem. We are pleased to have you with us this morning. I must remind the witnesses to please limit, again, your testimony to 5 minutes.

Our first witness, if you will come forward to the table now, is Dr. H. James Brown, director of the Joint Center for Housing Studies, Cambridge, MA.

Our next witness will be Robert R. McMillan, chairman of the Long Island Housing Association's Committee on Housing, Uniondale, NY.

And our final witness on this panel is Cathlene Wells, a teacher from the Los Angeles Public School System, Los Angeles.

We welcome you.

Well, unfortunately, there is a roll call. [Laughter.]

I have to go, and I will be back very, very shortly. We will adjourn momentarily.

[Recess.]

Senator CRANSTON. The hearing will reconvene. At this point I would like to insert statements of Senators Dixon, Sasser, and D'Amato.

STATEMENT BY SENATOR ALAN J. DIXON

Mr. Chairman, I wish to express my appreciation to you for directing the attention of this subcommittee to a growing national tragedy—the declining affordability of homeownership—with special emphasis on the first-time home buyer.

Homeownership is a concept that is deeply rooted in the heart of most Americans. The Federal Government has been actively involved in this concept of homeownership since the days of the depression either through tax benefits or other means. Homeownership is a major part of the American dream.

Studies show that in 1930, about 48 percent of American homes were owner-occupied. The depression brought on a decline to about 44 percent in 1940. However, in 1980, due primarily to Government-initiated programs, homeownership peaked at about 66 percent.

However, since 1980, overall homeownership has gradually declined. But we know that double-digit inflation and high interest rates have compounded the housing problem, resulting in many families having to find housing in a market that is far beyond their means.

Mr. Chairman, I look forward to hearing testimony this morning from these expert witnesses, including their proposals on how the Federal Government might ease the difficulties faced by today's first-time home buyers.

I am particularly interested in hearing testimony from Mr. H. James Brown of the Joint Center for Housing Studies regarding his findings as they relate to homeownership in the Midwest.

Thank you, Mr. Chairman.

STATEMENT OF SENATOR JIM SASSER

Mr. Chairman, today we consider an issue of critical importance to young Americans—homeownership affordability. We will hear today that the homeownership rate in this country is declining. Young Americans—first time home buyers—are being hit the hardest.

Indeed, affordable homeownership is becoming a contradiction in terms for Young Americans. In the 1950's a 30-year-old, average income head of household, spent roughly 14 percent of his income on his home mortgage. Today that same person spends over 44 percent of his income on his mortgage. And now I am afraid that rising interest rates will further choke off housing opportunities.

There are a lot of things going wrong out there. Stricter credit underwriting standards have all but eliminated the benefits to first-time home buyers of the lower interest rates of the past few years. Federal housing programs have been cut to the bone since 1980. The FHA has been repeatedly attacked by those seeking to terminate the enormous benefits provided by this program since the 1930's. And the tax reform bill of last year may have done serious long-term damage to the supply of housing for low income persons.

Mr. Chairman, America needs to renew its commitment to housing and homeownership. I am pleased that this committee is going to take a long hard look this issue over the months to come. Homeownership has been the bedrock of our society—we need to take action before this slips away.

STATEMENT BY SENATOR ALFONSE D'AMATO

Mr. Chairman, I am pleased that we are addressing the crucial issue of homeownership affordability. This is a fundamental issue for families and businesses. As a Senator from New York State, which has some of the highest housing costs in the Nation, I am all too aware of the housing affordability problem in this country.

Affordable housing is an increasing problem for individuals and families around the Nation. First-time home buyers especially have an extremely difficult time finding an affordable home. This is not without an immediate economic impact. Businesses and organizations cannot recruit employees if affordable housing is not available in the area.

Long Island is an excellent example of a difficult housing market. In the last 6 years, the median price of a home on Long Island has doubled—increasing from $63,000 to approximately $160,000. In the same 6 years, median family income has only risen from $29,000 to $43,000. That increase is clearly not enough to purchase a median-priced home.

The problem not only affects families moving into the Long Island market, but also senior citizens and young individuals buying a home for the first time. These three groups—the young, senior citizens, and new families moving into the community—are virtually shut out of the housing market on Long Island.

Housing trends suggest that Long Island's housing difficulties are not unique. Until 1980, the homeownership rate had increased steadily for 35 years. However, since 1980 this rate has fallen from

65.6% to 64.1%. This decline is primarily due to potential first-time home buyers opting to rent instead of purchase a home.

Homeownership rates among younger households—less than 35 years of age—have not only been declining since 1980, but they are now well below the 1980 level. Unless income levels of young adults rise substantially or the cost of homeownership declines, many more young families will be unable to purchase a home.

What are the economic ramifications? Businesses are forced to raise salaries to compensate for the high prices of homes. As prices continue to rise, housing costs become a key factor in business expansion decisions. Businesses cannot afford to expand in areas where housing is virtually unaffordable. Instead, businesses opt to expand in a different part of the country, or relocate their entire business elsewhere.

Homeownership is a fundamental personal and economic decision. I hope that this hearing will help provide better direction on how we can help assure individuals and families of affordable housing. With this direction, the subcommittee will be fully able to address this issue in Cranston-D'Amato legislation at the beginning of 1988.

Thank you, Mr. Chairman.

Senator CRANSTON. Thank you all for your patience, and we will hear first from Dr. H. James Brown.

STATEMENT OF H. JAMES BROWN, DIRECTOR, MIT-HARVARD JOINT CENTER FOR HOUSING STUDIES, CAMBRIDGE, CAMBRIDGE, MA

Dr. BROWN. Thank you, Senator. It is a real pleasure to be here today to participate in the hearings, representing the MIT-Harvard Joint Center for Housing Studies.

Over the past several years, we have been engaged in a very extensive study of the cost of homeownership. I have submitted the latest summary report of that work to the committee.

What we have been studying is not just the price of ownership but the full cost of owning, including the down-payment requirements and the utilities, taxes, maintenance, as well as the mortgage.

The results of these studies, I think, are quite alarming. Since 1980, the cost of homeownership, the full costs of homeownership, has risen substantially. Our estimate is that over this period, 1981 to 1986, the costs relative to income are more than three times the level of costs versus income in the 1970's.

It is important because this high cost of homeownership is not simply a problem of California or of the Northeast part of this country. These costs are high, by historical standards, in every region of the country. There are extremely serious cost versus income ratios throughout the country.

You might ask the question, how did these costs become so high? What is the nature of this problem, in terms of the high homeownership costs?

Part of the reason is the fact that housing prices have risen so rapidly over the last 10 years, caused to a certain extent by the rapid high cost of constructing new houses.

I might note, by the way, that the high cost of new construction is not the result of increases in material costs nor the cost of labor. The higher cost of construction is really a result of the high land prices, very high escalation in land prices, and the high financing costs for construction periods.

One cause, therefore, of high costs of housing is high prices of housing. But you also have to recognize a second factor, the high real interest rates.

These high interest rates mean that, relative to income, costs of housing have increased substantially.

And finally, I want to make note of the important problem of entry. The high down-payment and the high closing costs, mean that even when there are favorable opportunities for ownership, you have to have accumulated substantial capital, in order to enter homeownership.

What has been the impact of these high costs? You have raised the question yourself and pointed to what I think is probably the most significant impact of the high ownership, and that is the decline in homeownership rates.

As these diagrams indicate, and as you mentioned, for 35 years, homeownership rates have steadily increased. Since 1980, we have reversed that trend. Every year, homeownership rates have been declining.

Again, I want to point out that this is not simply a problem of the West or the Northeast. In every region of the country, we have experienced declining homeownership rates. It is important, when you see these gross numbers of decline in homeownership rates, to recognize that these rate declines are really the result of lower ownership rates for young households. Typically, older households who have bought don't have to respond to higher costs by moving to renter. They can stay in their homeownership.

The impact of the high cost of homeownership is direct on young households. The homeownership rates for 25- to 35-year-old households have dropped by more than 10 percent since 1981. I believe that this kind of drop for young households can have substantial social and economic impacts and it bodes a serious problem for this country.

I am happy to have been able to testify, and I will be happy to answer questions.

[The complete prepared statement of Dr. James Brown follows:]

SUPPLEMENT TO TESTIMONY BY DR. H. JAMES BROWN
for the SENATE SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS
WEDNESDAY, JULY 1, 1987

NOTE: Dr. Brown's testimony will be extracted from the report: "Home Ownership and Housing Affordability in the United States: 1963-1985"

NATIONAL HOMEOWNERSHIP RATE

In 1986, the nation's homeownership rate continued the decline that that began in 1981, staying below 64% for the first time in decades.

Home Ownership Rates:1973-1986

Year	All Households	Northeast	Midwest	South	West
1973	64.5	58.8	70.5	66.5	60.3
1974	64.6	58.8	70.4	66.3	60.6
1975	64.6	59.2	70.2	66.0	60.8
1976	64.7	59.8	69.7	66.4	60.9
1977	64.8	60.3	69.4	67.1	59.8
1978	65.0	60.6	69.3	67.9	59.2
1979	65.2	60.5	69.6	68.3	59.7
1980	65.6	60.8	69.8	68.7	60.0
1981	65.4	60.8	69.7	67.2	60.2
1982	64.8	61.1	69.4	66.7	59.4
1983	64.6	61.5	69.3	67.0	58.2
1984	64.5	61.2	68.4	67.0	58.5
1985	63.9	60.8	66.9	66.4	59.0
*1986	63.8	61.4	66.9	66.1	58.4

*estimates

EFFECT ON YOUNG HOUSEHOLDS

The decline in homeownership rates has been particularly sharp for young households. When homeownership rates are examined by age category, it is clear that the greatest declines are for households younger than 40.

AGE GROUP	1981	1982	1983	1984	1985	1986
ALL HOUSEHOLDS	65.4%	64.8%	64.7%	64.6%	64.1%	63.8%
Less than 25	20.7%	19.3%	18.8%	17.9%	17.4%	17.2%
25-29	41.7%	38.6%	38.3%	38.6%	37.7%	36.7%
30-34	59.3%	57.1%	55.4%	54.8%	54.7%	53.6%
35-39	68.9%	67.6%	66.5%	66.1%	65.7%	64.8%
40-44	73.7%	73.0%	72.8%	72.3%	71.8%	70.5%
45-49	76.2%	76.0%	75.2%	74.6%	74.9%	74.1%
50-54	78.3%	78.8%	78.8%	78.4%	77.4%	78.1%
55-59	80.0%	80.0%	80.1%	80.1%	79.1%	80.0%
60-64	80.0%	80.1%	79.7%	79.9%	79.6%	79.8%
65-69	77.6%	78.0%	78.7%	79.3%	79.4%	79.4%
70-74	75.4%	75.2%	75.3%	75.5%	76.7%	77.2%
More than 75	69.8%	71.0%	71.9%	71.5%	70.4%	70.0%

8

THE 1986 REPORT

Home Ownership
and
Housing Affordability
in the
United States:
1963-1985

Prepared by H. James Brown and John Yinger
of the Joint Center for Housing Studies
of the Massachusetts Institute of Technology
and Harvard University

Paper prepared for
National Gypsum Company
4500 Lincoln Plaza
500 North Akard Street
Dallas, Texas 75201
(214) 740-4500

Joint Center for Housing Studies
of the Massachusetts Institute of Technology
and Harvard University

SUMMARY

Although the cost of homeownership declined slightly in 1985, it remained much higher than its average for the previous 10 years (Exhibit 1). With affordability still a real problem, homeownership rates continued to fall.

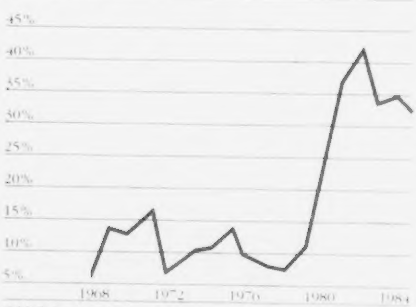
Last year more than 2.1 million new housing units were constructed in the United States. This was the third straight year of strong construction activity, reflecting both housing's continuing role in the current economic expansion and the strength of American demand for improved housing. But even in these good times, there are signs of a potentially serious problem: residential construction activity is being stimulated primarily by current owners moving up to a higher quality housing, whereas homeownership rates among younger households (less than 35 years of age) declined again in 1985 and are now well below the 1980 level. Unless young adults achieve substantial income growth or unless the cost of homeownership declines to more traditional levels, many more young families than in the past will find themselves unable to purchase a home.

The situation for renter households is even more ominous. Since 1974, the share of income that renters must devote to housing has risen dramatically: 47 percent of low income renters must now spend more than half of their income for rent, compared to 34 percent in 1974. Furthermore, even though approximately 5 million new multi-family units were built over the last decade, the number of structurally inadequate rental housing units actually increased over this period. In 1985, over 550,000 more low-income renters lived in structurally unsound housing than in 1974. Low income renters thus face declining housing quality *and* very high rent burdens, and current trends suggest that these problems may get worse.

This is the Joint Center for Housing Studies' third annual report on homeownership and housing affordability, a project undertaken for the National Gypsum Company. In addition to our general review of housing trends, we include a special section focusing on the rental housing market.

Exhibit 1

Cost of Home Ownership Index



SOURCE: See Appendix II

COST OF HOMEOWNERSHIP

High housing prices and interest rates have made it much more expensive to buy and maintain a home now than in the 1970s. This affordability problem is especially acute for first-time homebuyers, who must spend more than 30 percent of their income on housing. The heavy financial burden of owning is directly linked to the steady drop in the homeownership rate; today only 63.5 percent of all U.S. households are homeowners compared to 65.7 percent in 1980.

RECENT HOMEBUYERS

With home prices and interest rates stabilizing and the economy performing relatively well, households' income has grown steadily in the last few years. In 1985, the after-tax costs of purchasing (including mortgage payments, property taxes, and other out-of-pocket payments) for the typical homebuyer held at just over 31 percent of household income, compared with an average of about 26 percent in the early part of the 1970s and 35 percent in the early part of the 1980s. The total costs index (including an opportunity cost for the homeowner's equity and adjusting for appreciation in house values) skyrocketed in the 1980s and in 1985 remained at three times the average during the 1970s.

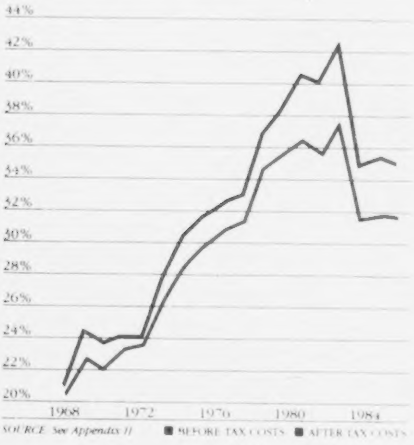
The median price of homes purchased during 1985 was up 4.3 percent from a year earlier — the largest increase during the decade but still substantially lower than the gains made during the last half of the 1970s. These higher prices not only mean higher mortgage payments but also larger downpayments. In 1978, the typical buyer had to make a downpayment of about one third of his or her household income; by 1985, the share had risen to 50 percent.

On the other hand, mortgage interest rates continued to decline last year, down from the high of 15.3 percent in 1982 to 11.27 percent. Lower interest payments reduce the size of

Exhibit 2

Tax Savings From Home-Ownership

Percentage of Income Recent Home Buyers

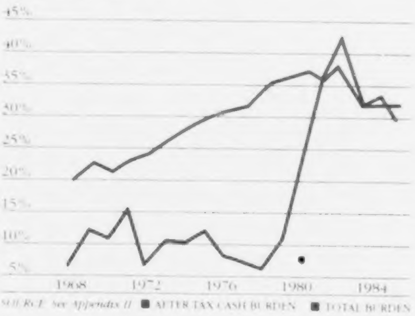


SOURCE: See Appendix II

Exhibit 3

Home Ownership Costs

Percentage of Income Recent Home Buyers



SOURCE: See Appendix II

Exhibit 4

Appreciation in House Values

	House Value[a]				Rates of Appreciation[b]				
	1968	1973	1980	1985	1968-73	1973-80	1980-85	1984-85	1968-85
Northeast	$20,000	$30,000	$51,300	$76,300	8.50%	8.00%	8.28%	13.00%	8.26%
Midwest	$17,500	$23,000	$48,000	$54,700	5.00%	11.10%	2.64%	3.20%	6.45%
South	$12,000	$18,000	$43,700	$56,700	8.50%	13.50%	5.34%	5.50%	9.11%
West	$18,000	$27,000	$77,700	$89,500	8.50%	16.30%	2.88%	-0.40%	9.23%
National	$16,500	$24,000	$51,300	$64,100	7.80%	11.50%	4.54%	4.30%	7.95%

a. Median value of all 1 unit owner-occupied houses
b. Average annually-compounded rate

monthly mortgage payments and roughly offset other cost increases over the year.

Contrary to popular wisdom, tax savings have a relatively modest impact on the cost of homeownership: the existing tax system lowers the cost of owning for the typical homebuyer by about 9 percent. The importance of the tax savings has increased, however, in recent years (Exhibit 2) and is significant for many first-time buyers.

The after-tax cash cost of purchasing a home for the typical buyer fell slightly last year from 31.99 to 31.79 percent of median income (Exhibit 3). The cash costs of purchasing have stabilized since 1983, but are still high by historical standards.

In determining the total cost of purchasing a home, it is necessary to allow for expected appreciation. Based on the experience of the past three years, a typical buyer can expect to receive a capital gain of about 3.6 percent per year. This gain is slightly higher than the gain received in the 1982-84 period, and the expected total cost of buying a residence is therefore lower.

The last element in calculating the total cost is the opportunity cost of revenue foregone from the capital used for the downpayment. If a household continued to rent, it could invest the downpayment and receive a return; giving up this return is part of the cost of buying.

Combining all these factors yields the total cost shown in Exhibit 3. Although it has come down from the extraordinary levels of the early 1980s, this home purchase cost remains high relative to its level in previous decades.

Surveys by the Joint Center and others suggest that young households feel thwarted by the high cost of homeownership and alarmed about their prospects of ever being able to buy. The survey results also indicate it is not only the monthly cash cost of ownership, but also the magnitude of the downpayment that is limiting the ability of an increasing proportion of young households to afford homeownership.

REGIONAL VARIATIONS IN PURCHASING COSTS

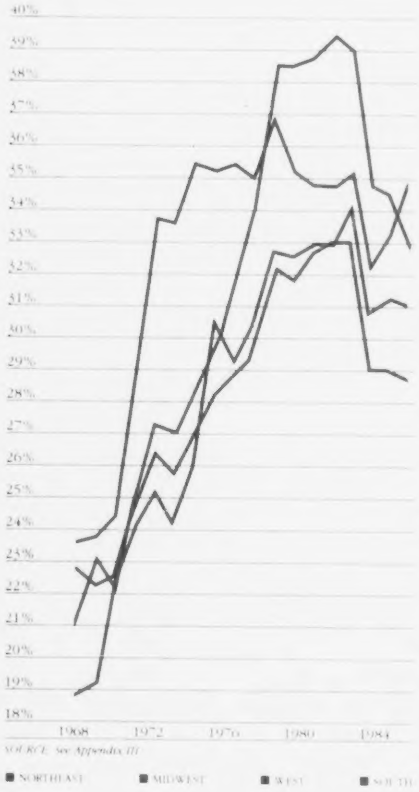
The cash and total costs of homeownership vary across regions and are directly related to the level of home prices and the expected rate of housing appreciation (Exhibit 4). While newly purchased homes appreciated 4.3 percent nationwide during 1985, the appreciation rate ranged from a 13 percent gain in the Northeast to a 0.4 percent decline in the West.

Last year housing price appreciation in the Northeast was much higher than in any other region and the most rapid of this decade. In the Midwest, home prices picked up somewhat

Exhibit 5

Regional Cash Ownership Costs

Percentage of Income



SOURCE: See Appendix III

from the poor performance in the early 1980s, but still lagged behind the national average. The South continued to see steady, solid increases in housing prices; last year's rise was somewhat higher than normal, but gains have varied much less from year to year than they have elsewhere in the country. The West, in contrast, experienced an absolute decline in the median price of homes sold. This drop reflects some of the economic problems facing the Northwest and the adjustment of California housing prices after the rapid appreciation of the late 1970s.

With these price changes, the cash cost of housing rose sharply in the Northeast, which replaced the West as the region with the highest cash costs (Exhibit 5).

Last year's appreciation in housing prices widened the spread of the total ownership costs across regions (Exhibit 6). The high cash costs in the West, combined with low appreciation, raised the total cost in this region even further; the West, therefore, remained the highest total cost area of the country. The rapid increases in the Northeast provided substantial gains from appreciation and a reduction in total costs. Because of the high costs in this region, which limit housing demand, housing appreciation in the Northeast is unlikely to continue at such a relatively high rate.

HOMEOWNERSHIP COSTS FOR CURRENT OWNERS

A current homeowner and a first time buyer obviously perceive the cost of homeownership quite differently. Existing homeowners have benefited from rapid price appreciation and are likely to find themselves in a strong financial position. The increases in the interest rates of the early 1980s did not affect the payments on mortgages written earlier. Similarly, the recent drop in interest rates has less effect on current owners' costs, although adjustable rate mortgages and the opportunity to refinance can lower the costs to those owners whose purchases were financed at higher rates. Refinancing had begun to increase in 1985 and is likely to pick up even more this year as interest rates continue to fall.

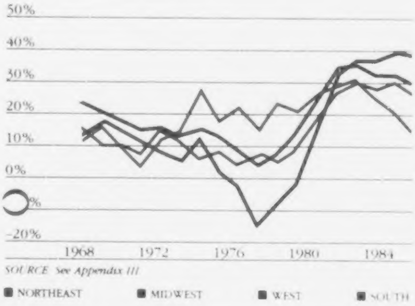
The cash cost of owning rose in 1985 — although less rapidly than household income. The cash burden of owning therefore declined somewhat (Exhibit 7). Note that the tax savings for the typical current owner are relatively small because interest payments are smaller on older mortgages. Of course, higher income owners with larger mortgages, higher property taxes, and higher marginal tax brackets have substantially greater tax savings than does the median homeowner. The claim that homeownership offers few tax advantages is confirmed by the fact that only about 40 percent of households who filed taxes in 1985 elected to itemize their deductions.

The total cost of maintaining ownership changed little last year (Exhibit 8). For the typical owner, the total costs (even accounting for potential appreciation) remained substantially above 1970s levels for the fifth year in a row.

Exhibit 6

Regional Total Ownership Costs

Percentage of Income

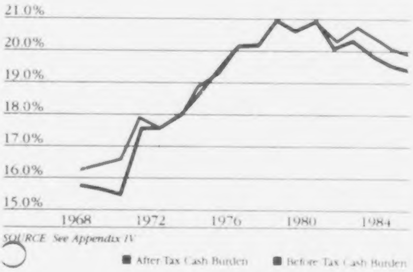


SOURCE: See Appendix III

Exhibit 7

Tax Savings from Homeownership

Percentage of Income/Non-movers

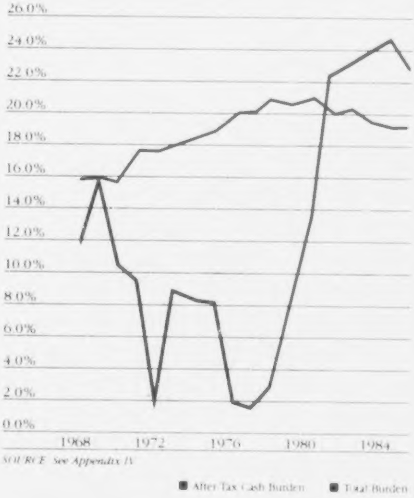


SOURCE: See Appendix IV

Exhibit 8

Homeownership Costs

Percentage of Income/Non-movers



SOURCE: See Appendix IV

IMPACTS OF THE HIGH COST OF HOMEOWNERSHIP

By some measures, American households are better off than they have been in almost a decade. The unemployment rate has fallen from a high of 9.5 percent in 1983 to 7.1 percent in 1986. Real per capita income has increased to its highest level ever, and median real family income has returned to the high level of 1980. Housing prices have stabilized, and the cash cost of owning a home has fallen with declining mortgage interest rates and the availability of new mortgage instruments. There is widespread optimism about the economy and about the future in general.

Even in these good times, however, serious problems remain. Homeownership rates have dropped for the last four years, particularly among young households. In 1985, the rate of default on home mortgages was at its highest level since the early 1970s. These problems are linked to the high cost of homeownership.

HOUSEHOLD FORMATION

The total number of households in the U.S. grew by about 1.4 million in 1984-85 (Exhibit 9), which was far above the extremely low growth in the early 1980s. This growth reflects both demographic factors, such as the aging of the baby boom generation, and the strength of the national economy, which enables many people to strike out on their own.

The proportion of the population in each age group that heads an independent household (the headship rate) also tends to vary with the cost of housing: when housing is less expensive, more individuals can afford to establish separate households rather than remain in group quarters with parents or friends. Between 1970 and 1980, the cost of homeownership (and, as will be shown below, the cost of rental housing) was relatively low, so headship rates for all age groups rose steadily (Exhibit 10). Since then, however, the cost of homeownership (and of rental housing) has risen sharply, thereby causing headship rates to decline. Indeed, headship rates for young households have returned to the level of the early 1970s. Gains in independent living achieved in the last decade have thus been lost.

Exhibit 9

Net New Households (1000s)

	75-80[a]	80-81[b]	81-82	82-83	83-84	84-85
Total	1,551	1,592	1,159	391	1,489	1,382
Family	595	759	710	374	604	710
Non-family	956	833	449	17	885	672
Singles	740	640	418	104	704	648
Two+	216	197	31	121	181	24

a. *Annual average growth*
b. *Counts from April to April*

SOURCE: U.S. Department of Commerce, Bureau of the Census, Current Population Reports, P-20 Series, various issues

Exhibit 10

Percentage of the Population who Head Their Own Households, 1970-1985

Age	1970	1975	1980	1981	1982	1983	1984	1985
15-24	12.6	15.1	15.9	15.7	15.0	14.2	13.9	14.0
25-29	45.2	47.8	48.4	48.3	47.2	45.9	46.8	45.9
30-34	48.9	52.0	53.3	53.2	53.0	51.5	52.1	52.2
35-44	50.8	52.3	54.9	55.2	55.9	55.7	55.2	55.9
45-54	52.5	54.8	55.6	56.4	56.0	55.6	56.1	56.4
55-64	58.3	58.3	58.3	58.5	59.2	59.5	59.6	59.0
65-74	62.4	66.8	65.8	65.9	66.1	66.4	65.9	70.7
75+	61.6	69.5	71.9	73.0	72.7	72.4	71.6	65.6

SOURCE: U.S. Department of Commerce, Bureau of the Census, Current Population Reports, P-20 Series, various issues

HOMEOWNERSHIP

Until 1980, homeownership rates had increased steadily for 35 years. Since the beginning of this decade, however, these rates have fallen every year for a total drop from 65.6 to 64.1 percent (Exhibit 11). Because households that own seldom revert to renting, most of this decline involves potential first-time buyers. Thus, as shown in Exhibit 12, the decline in ownership rates is greatest for young households.

The principal explanation for this decline is rapid growth in the price of homeownership relative to renting. During the 1970s, the real cost of owning was low and declining. According to the rental component of the consumer price index, rents also rose considerably more slowly than prices in general during the 1970s. Several recent studies have shown, however, that this index seriously overstates the relative decline in the price of rental housing because it ignores housing depreciation and the price of utilities not included in rents. Correcting for these two factors leads to the conclusion that the price of rental housing grew only slightly less than prices in general.[1] Throughout the 1970s, therefore, the relatively low price of homeownership encouraged households to purchase homes. Since 1980, both the cost of homeownership and the cost of rental housing have increased faster than prices in general. As documented earlier, the real cost of homeownership grew dramatically in the early 1980s. The real cost of renting grew more slowly and by 1984 was about 8 percent above its 1980 level.[2] Thus, the cost of homeownershp has increased significantly relative to the cost of renting, thereby discouraging many young households from purchasing a home.

A second possible explanation for the recent drop in homeownership is that young households may have developed new life styles or work habits that make ownership less desirable. While changes in living arrangements and labor-force participation have indeed occurred in the past 20 years, they have been gradual and cannot explain the sudden decline in homeownership rates since 1980,

MORTGAGE DEFAULTS

In 1985, the default rate rose to almost 1 percent of existing mortgages, the highest in over a decade. Nearly 6 percent of all home mortgage borrowers were at least 30 days late on a monthly payment (Exhibit 13). The foreclosure rate has nearly doubled since 1980 from .13 percent to .25 percent of all mortgages in 1984 and 1985. More than $500 million was paid by the 13 largest mortgage insurers, about 10 times the amount paid in 1980. These developments indicate a large and growing problem of mortgage default and delinquency in the U.S.

Exhibit 11

Home Ownership Rates: 1973-1985

Year	All Households	Northeast	Midwest	South	West
1973	64.5	59.2	69.1	66.5	60.6
1974	64.6	59.3	69.2	66.7	61.1
1975	64.6	59.5	69.4	66.4	61.1
1976	64.7	59.7	69.3	66.4	61.3
1977	64.7	59.3	69.3	66.8	61.4
1978	65.0	59.9	70.2	67.3	60.8
1979	65.2	59.9	70.3	68.2	60.5
1980	65.6	60.7	70.1	68.3	60.4
1981	65.4	61.3	70.2	67.4	59.8
1982	64.8	61.1	69.4	66.7	59.4
1983	64.7	60.4	69.1	67.4	59.0
1984	64.6	61.1	68.6	66.8	59.4
1985	64.1	60.9	67.3	66.7	59.2
Changes					
1973-1980	+1.1	+1.5	+1.0	+1.8	-0.2
1980-1985	-1.5	+0.2	-2.8	-1.6	-1.2

SOURCE: *U.S. Department of Housing and Urban Development, Annual Housing Survey and Current Housing Reports, H-111 Series, various issues.*

Exhibit 12

Percent of U.S. Homeownership by Age of Householder

Age	1981	1982	1983	1984	1985
Total	65.4	64.8	64.6	64.5	64.1
Less than 25	20.7	19.3	18.8	17.9	17.4
25-29	41.7	38.6	38.3	38.6	37.7
30-34	59.3	57.1	55.4	54.8	54.7
35-39	68.9	67.6	66.5	66.1	65.7
40-44	73.7	73.0	72.8	72.3	71.8
45-49	76.2	76.0	75.2	74.6	74.9
50-54	78.3	78.8	78.8	78.4	77.4
55-59	80.0	80.0	80.1	80.1	79.1
60-64	80.0	80.1	79.7	79.9	79.6
65-69	77.6	78.0	78.7	79.3	79.4
70-74	75.4	75.2	75.3	75.5	76.7
75 or more	69.8	71.0	71.9	71.5	70.4

SOURCE: Economic News Notes, *National Association of Home Builders, January 1986.*

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[1] *Rental Price indexes through 1984 are presented in National Association of Home Builders, "Low and Moderate Income Housing: Progress, Problems and Prospects," January 1986.*

[2] *Ibid.*

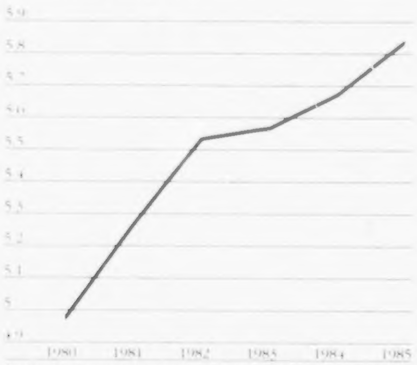
Part of the explanation for this problem is uneven economic growth. While the national economy has been growing steadily, several state economies have suffered serious setbacks. For example, the declining price of oil has resulted in a slump in some southern states and thereby limited income growth and the ability of households to maintain monthly mortgage payments. As a result, default rates in the South have been steadily increasing in recent years.

Changes in the mortgage market also help to explain the increase in defaults. Some institutions offer new mortgage instruments with payments that increase over time, and many lenders have raised the amount they will lend a person with a given income. These changes make homeownership more accessible to many households. Nevertheless, households whose incomes do not grow may find themselves unable to meet increasing mortgage payments and increasing the amount a household can borrow also increases its vulnerability to a deterioration in its economic circumstances.

Finally, the high rates of default and delinquency are related to the combination of high homeownership costs and declining housing appreciation. Many households purchased housing with the expectation that appreciation in house values would provide an investment return to justify the high costs. Because mortgage lenders also anticipated high appreciation, many of them issued mortgages with low downpayment requirements. In many regions, however, actual housing appreciation has been much lower than expected, so households with low downpayments — and hence with little equity to lose — have found it economical to default on their mortgage rather than maintain their monthly payments.

Exhibit 13

Annual Delinquency Rates*



*NOTE: The annual rate is an average of all 30-day, 60-day, and 90-day past due mortgages and mortgages in foreclosure.

SOURCE: *Mortgage Bankers Association, National Delinquency Survey*, various issues.

HOUSING CHOICE

With mortgage interest rates falling and the economy still expanding, 1985 was a strong year for housing construction with over 2.1 million units started or put on site (Exhibit 14). Much of this activity was generated by trade-up buying as current owners purchased bigger homes with more amenities (Exhibit 15). The proportion of new units that were single family increased to 52.3 percent.

While the extensive construction activity and the improvement in the quality of new units seem to contradict the evidence of higher housing costs, in fact they simply emphasize the different circumstances of first-time buyers and of current owners. Current owners who have accumulated substantial equity in their units have increasingly taken the opportunity offered by interest rate declines to improve their housing. Trade-up buyers are therefore the main source of demand for new construction. First-time buyers, in contrast, are hard pressed by the higher downpayment requirements caused by the steady increase in house prices. The increasing share of trade-up buyers thus indicates the relatively strong position of current owners and the weakening position of first-time buyers.

These developments are troubling because the long-run strength of the housing construction industry depends on the demand of young and other potential first-time buyers. In the future, the high cost of homeownership may limit this demand and impose severe constraints on the construction of single-family housing.

Exhibit 14

New Housing Units by Type
as Percent of Total Private Housing Starts

Year	Single Family Units	Condominiums	Other Units	Mobile Home Shipments	Total Starts (000s)
1973	38.4	9.6	29.5	22.5	2,515
1974	50.1	10.5	19.3	20.0	1,659
1975	62.3	4.7	16.3	16.7	1,371
1976	63.8	5.2	17.2	13.8	1,810
1977	62.7	5.9	19.9	11.5	2,236
1978	60.7	6.9	20.1	12.3	2,268
1979	57.0	9.9	19.0	14.1	1,990
1980	53.6	12.4	18.4	15.6	1,502
1981	51.5	14.0	17.1	17.7	1,291
1982	47.5	13.2	21.1	18.2	1,280
1983	50.0	14.0	22.0	14.0	1,981
1984	48.6	14.3	23.2	13.9	2,032
1985	52.3	10.6	23.8	13.3	2,130
Average					
1973-1985	53.1	10.1	20.5	15.7	1,852

SOURCE: U.S. Department of Commerce, Bureau of the Census, Construction Reports, C-20 Series, various years.

Exhibit 15

Selected Characteristics of New Privately Owned
Single Family Homes Completed 1968-1985

	1968	1970	1975	1979	1980	1981	1982	1983	1984	1985
Median Number of Square Feet	1,500	1,385	1,535	1,645	1,595	1,550	1,520	1,565	1,605	1,605
Percent with two or more Bathrooms	54%	48%	60%	74%	73%	70%	67%	72%	76%	77%
Percent with a Garage	66%	58%	67%	73%	69%	67%	65%	68%	70%	70%

SOURCE: U.S. Department of Commerce, Bureau of the Census, Construction Reports, C-25 Series, various years.

1985 SPECIAL FOCUS SECTION:

THE RENTAL HOUSING MARKET[3]

The last 12 years have been a period of substantial change for the rental housing market. While the number of renter households rose throughout this period, the growth was erratic. In the 1970s, the relatively low price of owner-occupied housing attracted many households to homeownership. In the 1980s, the rapid rise in the cost of homeownership pushed many households back into the rental market. This period also witnessed an increase in the number of structurally inadequate rental housing units and a striking increase in the share of income that renter households had to devote to rent and heat. Both of these developments have had a particularly severe impact on low-income households.

THE CHANGING CHARACTERISTICS OF RENTER HOUSEHOLDS

In 1983, 35 percent of U.S. households rented their housing — the same percentage as in 1974. As shown in Exhibit 16, the share of renters was particularly high among single and unrelated adults (52 percent), single parents (64 percent), and households with heads less than 25 years old (81 percent). Not surprisingly, therefore, over half of all renter households are single or unrelated adults, and over half are between the ages of 25 and 44.

Low-income households are also much more likely to rent than are high-income households. For the purposes of this report, income classes are based on the quartiles of the 1974 household income distribution. For example, households in the lowest income class in each year have the same real income as households in the bottom quartile of the household income distribution in 1974.[4] With this approach, 55 percent of the households in the lowest income class in 1983 were renters, compared to only 21 percent in the highest income class (Exhibit 16). As a result, households in the lowest income class made up 40 percent of all renter households.

A variety of social, demographic, and economic factors influence the process of household formation. During the 1970s, many members of the baby boom generation formed households as they entered their twenties. The number of renter households equals the total number of households multiplied by the share of households that decide to rent. This share is influenced by such factors as the cost of renting relative to owning. Although the number of households grew rapidly between 1974 and 1983, trends in the share of households that rent were quite different before and after 1980. Before 1980, the low relative price of owner-occupied housing lowered the share of renters in most household categories; after 1980, however, the dramatic increase in the relative price of owner-occupied housing raised the renter shares.

Between 1980 and 1983, the overall growth in households was 6 percent — about half the annual growth rate between 1974 and 1983. Household growth was concentrated in the 35-44 age group (with an 18 percent increase in households) and by the elderly (with a 9 percent increase). The growth in these age cohorts also led to more single and unrelated adult households and to more single-parent households. In terms of income, household growth occurred in all income classes but was highest in the top and bottom classes — as it was between 1974 and 1980.

The share of households that rent increased from 34.4 to 35.3 percent between 1980 and 1983 — exactly offsetting the decline between 1974 and 1980. Single adults and couples without children continued to move into ownership — but at a slower rate than in the 1970s. All other household types, however, experienced increases in the renter share, with the biggest growth for couples with children. Among age brackets, only the elderly saw a decrease (5 percent) in renter share. Finally, there was a shift toward renting in all income classes. The highest income class experienced a large increase in renter share (5 percent) — a striking turnaround from the 19 percent decline in its renter share between 1974 and 1980.

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[3] *Detailed data in Appendices V-VII.*

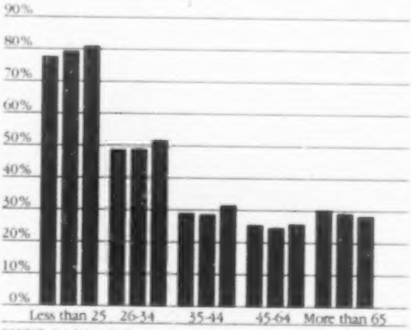
[4] *To facilitate comparisons across households of different sizes, total household income is divided by a household size equivalent, namely $[1 + 1/3(N-1)]$, where N is total household size. This approach approximates the household size equivalents used to define the 1984 poverty lines for households of different sizes. See U.S. Bureau of the Census, "Estimates of Poverty Including the Value of Non-Cash Benefits: 1984," Technical Paper No. 55, 1985). The role of income is essentially the same if total household income is used instead of this adjusted household income.*

The net effect of this growth in total households and the general shift toward renting between 1980 and 1983 was an increase in the number of renters in virtually every household category. All household types saw an increase, with the largest growth among married couples with children. All age brackets except the youngest saw an increase, with the biggest jump (31 percent) in the baby boom group aged 35-44. And all income classes saw an increase in renter households ranging from 2 percent in the second class to 21 percent in the highest class. This rapid growth in the highest income class is a reversal from the 1974-80 period, when many high income people switched into homeownership. This growth also represents a significant spreading out of the household income distribution for renters.

Exhibit 16

Percentage of Households That Rent

By Age of Household Head



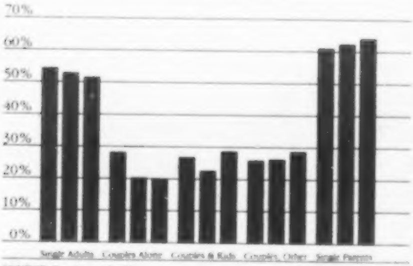
SOURCE: See Appendix V

■ 1974 ■ 1980 ■ 1983

Exhibit 16

Percentage of Households That Rent

By Household Type

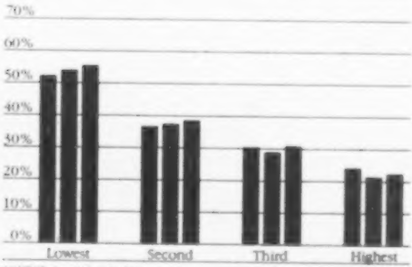


SOURCE: See Appendix V

Exhibit 16

Percentage of Households That Rent

By Income Class



SOURCE: See Appendix V

■ 1974 ■ 1980 ■ 1983

CHANGES IN RENTAL HOUSING QUALITY

The 1970s were a decade of extensive public and private housing construction. Rental housing starts fell from about 620,000 units in 1972 to 220,000 units in 1979; however, this decline was offset to some degree by an increase in "non-new" housing additions — units converted from nonresidential use, added to existing buildings, or returned to the housing stock after being temporarily removed. Subsidized housing starts averaged about 250,000 units annually at the beginning of the decade, only 54,000 units in 1974, and about 172,000 units annually in 1978 and 1979.[7] After slowing in the early 1980s, multifamily construction, which constitutes most of rental housing starts, has now returned to the levels of the late 1970s (Exhibit 14).

As new housing was built, some of the lowest-quality units were removed from the stock. It is not surprising, therefore, that the incidence of serious housing deficiencies declined over the 1974-83 period: the share of rental housing units lacking complete plumbing dropped from 5.4 percent to 2.9 percent, the share lacking a private bath dropped from 6.1 percent to 5.0 percent, and the share with more than one person per room dropped from 7.0 percent to 5.2 percent. On the other hand, the share of rental units that lacked heat rose from 1.2 percent to 1.4 percent.

To some degree, however, the lower incidence of some housing defects reflects the growth in the total number of renter households — not a decline in the number of renter households in housing with these defects. The number of renter-occupied housing units increased 19 percent between 1974 and 1983. With this change alone, the share of rental housing units that lack complete plumbing would have dropped to 4.5 percent, that lack a private bath to 5.1 percent, and that have more than one person per room to 5.8 percent.

Furthermore, focusing on a single serious defect ignores the obvious fact that housing defects take different forms in different units. Some apartments are inadequate because they do not have complete plumbing, while others are inadequate because they have holes in the roof. A recent Joint Center study developed an index of structural inadequacy that accounts for a variety of structural defects in housing.[8] To be specific, a unit is deemed inadequate if it has serious problems, such as frequent breakdowns, a lack of complete equipment, or a need for major repairs, in its plumbing, heating, electricity, roof, walls, hallways, or kitchen.

Using this index of housing inadequacy yields much more discouraging results than the simple indicators discussed above. Between 1974 and 1983, the percentage of renter households living in inadequate housing declined from 14.5 to 12.8. Because of the large growth in number of renter households, however, the number of renter households in inadequate housing actually rose by nearly 7 percent, from 3.60 million to 3.85 million. The increase in structural inadequacy occurred even though many substandard units were removed from the housing stock between 1974 and 1983. Indeed, these results imply that for every 100 inadequate units that were taken off the market during this period, 107 other units slipped into the inadequate category because of a lack of maintenance and upkeep.

Not surprisingly, changes in the extent of housing inadequacy varied widely by household type, age, and income. Those groups particularly at risk are single-parent families, low-income households, and households in the 25-34 age bracket (Exhibit 15). For example, 177,000 more single-parent families and 334,000 more low-income families resided in inadequate housing in 1983 than in 1974.

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[7] For a more complete discussion of construction activity in the 1970s, see Anthony Downs, *Rental Housing in the 1980s* (Washington, D.C.: Brookings, 1983).

[8] See William C. Apgar, Jr., "Recent Trends in Housing Quality and Affordability: A Reassessment," MIT-Harvard Joint Center for Urban Studies Working Paper No. W85-1, 1985.

THE RAPID INCREASE IN RENT BURDENS

Perhaps the most striking feature of the 1974-83 period in the rental housing market was the steady, rapid increase in rent burdens, i.e., in rents plus heating payments as a percentage of household income. The median rent burden went from 20 percent of income in 1970, to 27 percent in 1980, to 29 percent in 1983. Furthermore, the share of households with rent burdens below one quarter of their income dropped from 60 percent in 1974 to 40 percent in 1983. The share of households with rent burdens above seventy-five percent of income rose from 8 percent to 13 percent.

The changes in the rent burden distribution for the poorest households were particularly dramatic. In 1974, the median rent burden for households in the lowest income class was 35 percent of income. By 1983, the median rent burden for households in this income class had risen to 46 percent of income, and over one-quarter of the households in this class had rent burdens above three quarters of income. The median rent burden in the second income class rose from 21 percent of income in 1974 to 27 percent of income in 1983. In addition, this income class experienced a large increase in the number of households with rent burdens between 25 and 50 percent of income. By 1983, almost half of the households in this class had rent burdens of this magnitude. These shifts are illustrated in Exhibit 18.

While rent burdens rose in all locations, the increase was somewhat higher for residents of central cities, where rent burdens were the most onerous to begin with. The median rent burden for blacks remained about 3 percentage points higher than for whites.

These results must be interpreted with great care for two reasons. First, some households fall temporarily into the lowest income class because of illness or the loss of a job. For these households, high rent burdens do not persist but do add to the difficulty of recovering from unfortunate circumstances. On the other hand, high rent burdens represent an ongoing problem for the long-term poor.

Second, these rent burdens are based on households' cash income and therefore exclude income in kind, such as food stamps and Medicaid. Between 1974 and 1980, the in-kind benefits received by households, particularly low income households, increased significantly. As a result, the figures cited above overstate the increase in rent burdens as a percentage of total income. While the exact increment to income from in-kind benefits is difficult to determine, one study estimates that including all such benefits reduces the median rent burden in the lowest one fifth of the income distribution from 62 percent to 49 percent.[7] For the second fifth, the drop in median rent burden would be from 30 percent to 27 percent. In-kind income does make a difference, but even accounting for in-kind transfers, rent burdens in this lowest income class are now at extremely high levels.

It is important to note, however, that in-kind transfers stopped rising in 1980. Indeed, the real market value of non-cash transfers declined 4 percent between 1980 and 1983. The value of non-cash transfers per household declined by even more because the number of recipients also increased over this period.[8] The above results therefore understate the increase in rent burdens between 1980 and 1983.

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[7] *National Association of Home Builders, "Low and Moderate Income Housing."*

[8] See *U.S. Census Bureau, "Estimates of Poverty Including the Value of Non-Cash Benefits: 1984."*

Recent increases in rents as a fraction of income could, in principle, reflect improvements in housing quality. The evidence does not support this possibility. The number of households — particularly at the bottom of the income distribution — residing in structurally [illegible] Furthermore, it appears that rents have increased the most rapidly for lower income households. One recent study found that between 1974 and 1983, renter households with 1974 incomes below $5,000 saw a median increase in real rent of 9.9 percent and renter households with 1974 incomes between $5,000 and $10,000 saw a median increase of 9.6 percent.[9] Over the

Exhibit 17

Renters With Inadequate Housing

By Household Type

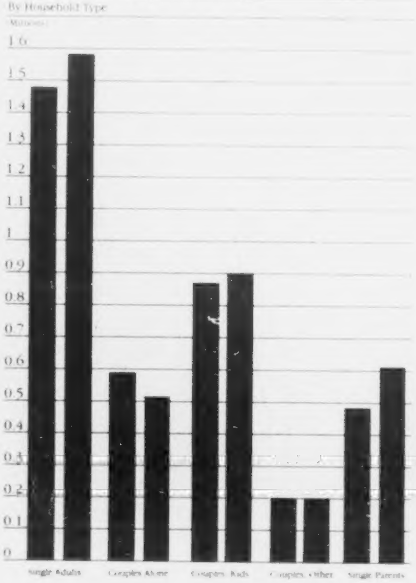
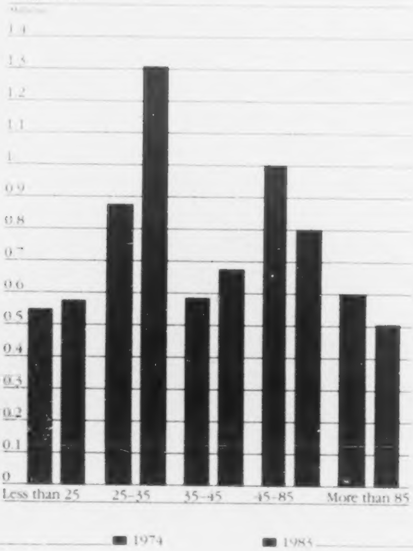


Exhibit 17

Renters With Inadequate Housing

By Age Bracket



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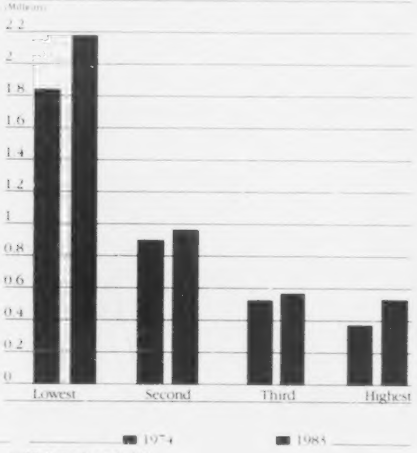
[9] *National Association of Home Builders, "Low and Moderate Income Housing."*

same period, real rents for households in the $20,000–30,000 income class rose just 2.3 percent and those for renters with incomes above $30,000 were unchanged. The higher rent burdens for low-income households therefore primarily reflect a rapid growth in the amount these households must pay for housing of any given quality.

Exhibit 17

Renters With Inadequate Housing

Income Class



SOURCE: See Appendix VII

Exhibit 18

Percentage Distribution of Rent Burdens

All Renter Households

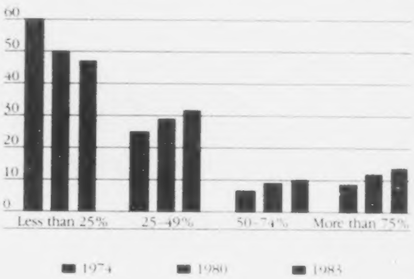
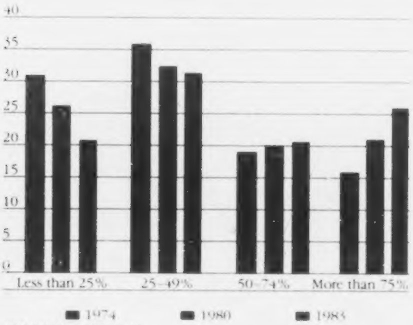


Exhibit 18

Percentage Distribution of Rent Burdens

Lowest Income Class



SOURCE: See Appendix VI

CONCLUSIONS

The good news in the housing market, namely the continuing high levels of construction, masks serious bad news brought on by the high cost of homeownership. Many young families are unable to afford homeownership and many current owners are finding it difficult to make their mortgage payments. The cost of homeownership declined slightly in 1985, but remained over 30 percent of the typical homebuyer's income—a very high number by historical standards. And the rate of mortgage defaults was at its highest level in over ten years.

Two developments have kept this situation from becoming even worse: changes in the mortgage market and the construction of condominiums. Some new mortgage instruments allow payments to increase over time as the borrower's income increases. Mortgage qualifying guidelines have been relaxed, thereby allowing households to borrow more money at a given income level. These changes ease young families' entry into homeownership but also raise the probability of default if their incomes do not rise. Further, condominiums tend to be smaller and less expensive than single-family houses, so the construction of condominiums allows some young families to become homeowners and to begin to accumulate housing equity, even if they cannot afford a single-family house. If the cost of homeownership does not decline in the future, a condominium may become the first home purchased by the typical family.

The cost of rental housing also has risen in recent years, resulting in very high rent burdens for low-income households. These high rent burdens drain the resources low-income households need to improve their economic situation and make it difficult for them to move out of inadequate housing. Whether this serious social problem will abate or worsen in the years ahead depends on the state of the national economy, the characters and magnitude of future federal housing subsidies, and the tax treatment of rental housing that emerges from the current congressional debate over tax reform.

Appendix I

Housing Market Indicators, 1968-1985

Year	Private Housing Starts[1]	Existing Home Sales[2]	Contract Mortgage rate[3]	Household Income (median)[4]	New Home Constant Quality Price[5]	New Home Actual Price[5]	CPI Overall[6]	CPI Owners[6]		CPI Renters[6]		U.S. Total Number of Households[7]	Average Household Size[7]
1968	1,507,600	1,569,000	7.03%	7,743	27,100	26,600	104.2	105.7		102.4		60,813	3.20
1969	1,466,800	1,594,000	7.82%	8,389	29,200	27,900	109.8	116.0		105.7		62,214	3.16
1970	1,433,600	1,612,000	8.36%	8,734	30,000	26,600	116.3	128.5		110.1		63,401	3.14
1971	2,052,200	2,018,000	7.67%	9,028	31,600	28,300	121.3	133.7		115.2		64,778	3.11
1972	2,356,600	2,252,000	7.51%	9,697	33,600	30,500	125.3	140.1		119.2		66,676	3.06
1973	2,045,300	2,334,000	8.01%	10,512	36,000	35,500	133.1	146.7		124.3		68,251	3.01
1974	1,337,700	2,272,000	9.02%	11,197	40,000	38,900	147.7	163.2		130.6		69,859	2.97
1975	1,160,400	2,452,000	9.05%	11,800	44,300	42,600	161.2	181.7		137.3		71,120	2.94
1976	1,537,500	3,002,000	9.08%	12,686	48,100	48,000	170.5	191.7		144.7		72,867	2.89
1977	1,987,100	3,547,000	9.02%	13,572	54,200	54,200	181.5	204.9		153.5		74,142	2.86
1978	2,020,300	3,863,000	9.56%	15,064	62,100	62,500	195.4	227.2		164.0		76,030	2.81
1979	1,745,100	3,701,000	10.87%	16,461	70,900	71,800	217.4	262.4		176.0		77,330	2.78
1980	1,292,200	2,881,000	12.84%	17,710	78,700	76,400	246.8	314.0		191.6		80,776	2.76
1981	1,084,200	2,418,000	14.91%	19,074	85,300	83,000	272.4	352.7		208.2		82,368	2.73
1982	1,062,200	1,991,000	15.31%	20,171	87,000	83,900	289.1	376.8	100.0	224.0	100.0	83,527	2.72
1983	1,703,000	2,719,000	12.73%	20,885	89,700	89,800	297.1	382.0	102.5	236.3	103.0	83,918	2.73
1984	1,749,500	2,868,000	12.04%	22,415	93,200	97,600	311.1	[illegible]	107.3	248.6	108.6	85,407	2.71
1985	1,736,400	3,214,000	11.27%	NA	95,200	99,200	322.4	NA	113.2	264.6	115.4	86,789	2.69

SOURCES: HOUSING MARKET INDICATORS

1. *U.S. Department of Commerce, Bureau of the Census:* Construction Reports, Housing Starts, Series C-20.
2. *National Association of Realtors,* Existing Home Sales.
3. *U.S. Federal Home Loan Bank Board.*
4. *U.S. Department of Commerce, Bureau of the Census:* Current Population Reports, Consumer Income, Series P-60.
5. *U.S. Department of Commerce, Bureau of the Census:* Construction Reports, Price Index of New One-Family Houses Sold, Series C-27.
6. *U.S. Department of Labor, Bureau of Labor Statistics:* CPI Detailed Reports. *The BLS has recently revised its method of computing homeownership and rental costs. New base is 1982 = 100.0.*
7. *U.S. Department of Commerce, Bureau of the Census:* Current Population Reports, Population Characteristics, Series P-20.

Appendix II

Housing Costs, 1968–1985, All Recent Purchasers

Year	House Value (median)	After Tax Mortgage payment	After Tax Property tax	Utility payment	Marginal tax rate	Household Income (median)	Standard Deduction[2]	Insufficient Deductions[3]	Tax Savings[4]	Appreciation[5]	Equity[6]	Opportunity Cost of Equity[7]
1968	15,000	681	212	350	18.5%	9,000	1,000	550	78	1,533	6,400	294
1969	17,600	884	205	350	19.0%	9,300	1,000	535	130	1,300	6,833	391
1970	17,900	1,015	225	350	20.0%	10,400	1,000	471	190	1,500	7,700	425
1971	19,500	1,182	240	350	20.0%	11,000	1,500	950	118	1,133	8,000	512
1972	21,000	1,353	271	370	20.5%	11,800	2,000	1,405	56	2,367	10,033	396
1973	25,000	1,608	290	420	20.5%	12,300	2,000	1,385	132	2,600	11,700	680
1974	27,300	1,935	324	600	21.0%	13,700	2,000	1,315	251	3,333	14,467	935
1975	31,000	2,311	394	650	22.0%	15,200	2,600	1,840	244	3,333	15,500	750
1976	35,000	2,506	421	730	22.5%	16,300	2,800	1,985	273	4,233	17,333	742
1977	40,000	2,831	478	770	22.5%	17,900	3,200	2,305	291	5,000	18,800	832
1978	46,000	3,383	472	880	23.0%	18,700	3,200	2,265	475	6,467	21,700	1,293
1979	54,400	3,754	475	900	24.0%	20,200	3,400	2,390	581	6,800	23,400	1,754
1980	60,400	4,192	479	1,085	25.0%	21,900	3,400	2,305	789	4,867	25,233	2,061
1981	60,600	4,691	491	1,070	26.0%	24,000	3,400	2,200	1,048	2,700	27,233	2,648
1982	62,500	5,158	547	1,200	25.0%	24,800	3,400	2,160	1,175	1,467	30,033	2,494
1983	64,800	4,204	576	1,200	24.0%	26,800	3,400	2,060	859	2,033	32,133	2,149
1984	66,700	4,620	588	1,320	23.5%	28,400	3,400	1,980	992	2,033	33,273	2,530
1985	69,600	4,544	612	1,340	24.0%	29,025	3,400	1,949	1,013	2,567	33,946	2,175

Housing Costs, 1968–1985, All Recent Purchasers

Year	Maintenance & Repairs[8]	Insurance[9]	Transaction Costs[10]	After Tax Cash Costs of Ownership[11]	Total Costs of Ownership[12]	Cash Costs Burden	Total Costs Burden
1968	150	75	350	1,817	577	20.19%	6.41%
1969	176	88	411	2,115	1,205	22.74%	12.96%
1970	179	90	418	2,276	1,201	21.89%	11.55%
1971	195	98	455	2,520	1,698	22.90%	15.44%
1972	210	105	490	2,799	828	23.52%	6.95%
1973	250	125	583	3,276	1,356	26.64%	11.02%
1974	273	137	637	3,906	1,507	28.51%	11.00%
1975	310	155	723	4,544	1,970	29.90%	12.96%
1976	350	175	817	4,998	1,506	30.66%	9.24%
1977	400	200	933	5,612	1,444	31.35%	8.07%
1978	460	230	1,073	6,498	1,325	34.75%	7.09%
1979	544	272	1,269	7,215	2,148	35.72%	10.64%
1980	604	302	1,409	8,072	5,266	36.86%	24.04%
1981	606	303	1,414	8,575	8,523	35.73%	35.51%
1982	625	313	1,458	9,281	10,308	37.42%	41.56%
1983	648	324	1,512	8,525	8,641	31.81%	32.24%
1984	667	334	1,556	9,085	9,582	31.99%	33.74%
1985	696	348	1,624	9,163	8,772	31.57%	30.22%

SOURCES: HOUSING COSTS, RECENT PURCHASERS
Unless otherwise noted, data for 1968-1972 are median figures compiled from the Panel Study of Income Dynamics, *Institute for Social Research, University of Michigan. Data for 1973-1981 and 1983 are from the* Annual Housing Survey, *U.S. Department of Commerce, Bureau of the Census.*

[1] Statistical Abstract of the U.S. — *1984*

[2] U.S. Master Tax Guide, *Chicago: Commerce Clearing House, Inc.*

[3] *Estimated as standard deduction amount minus 5% of homeowner income*

[4] *Estimated as (MI + PT) − ID)* MTR*
where MI = mortgage interest payments
PT = property tax payments
ID = insufficient deductions
MTR = household marginal tax rate

[5] *Three year moving average used*

[6] *All years estimated from the PSID, 3 year moving average used*

[7] *Opportunity cost of the homeowner's equity calculated using yield from 1 year U.S. Treasury Bonds as reference, as reported in* Federal Reserve Bulletin

[8] *Estimated as 1% of house value*

[9] *Estimated as 0.5% of house value*

[10] *Estimated as 7% of house value averaged over a three year period*

[11] *Sum of net mortgage payments, net property taxes, utility payments, maintenance and repair expenditures, insurance payments and transaction costs*

[12] *Cash costs plus appreciation, minus opportunity cost of equity*

Appendix IIIa

Housing Costs, 1968-85, Region: Northeast (Recent Purchasers)

Year	House Value (median)	After Tax Mortgage payment	After Tax Property tax	Utility payment	Household Income (median)	Tax Savings	Appreciation	Equity	Opportunity Cost of Equity
1968	20,000	814	289	350	9,500	136	1,500	7,247	330
1969	21,500	939	288	350	10,200	179	1,167	7,260	413
1970	22,000	1,071	308	450	10,900	231	2,000	6,747	372
1971	26,000	1,410	358	498	11,200	207	2,833	5,567	217
1972	30,000	1,777	413	522	11,500	197	2,667	5,220	206
1973	30,000	1,700	440	553	11,700	202	2,333	5,710	332
1974	33,000	2,080	557	780	13,200	345	1,667	6,410	414
1975	35,000	2,362	614	885	14,800	297	2,667	7,070	351
1976	38,000	2,476	663	975	15,700	317	2,333	7,693	331
1977	40,000	2,592	755	1,000	16,800	287	3,333	9,043	400
1978	45,000	2,985	757	1,005	17,500	411	3,100	12,217	733
1979	47,300	2,937	789	1,188	19,100	383	3,767	17,150	1,288
1980	51,300	3,142	804	1,450	21,200	521	3,700	22,676	1,864
1981	56,100	3,716	846	1,400	23,400	777	3,900	25,889	2,551
1982	59,000	4,103	858	1,562	25,000	937	3,533	28,133	2,336
1983	61,900	3,447	944	1,650	26,500	728	3,800	28,607	1,913
984	67,500	3,970	969	1,720	27,800	925	5,767	30,242	2,285
1985	76,300	4,167	1,086	1,748	28,412	1,934	7,733	30,814	1,974

Housing Costs, 1968-85, Region: Northeast (Recent Purchasers)

Year	Maintenance & Repairs	Insurance	After Tax Cash Costs of Ownership	Total Costs of Ownership	Cash Costs Burden	Total Costs Burden
1968	200	100	2,220	1,050	23.37%	11.05%
1969	215	108	2,402	1,648	23.54%	16.15%
1970	220	110	2,673	1,045	24.52%	9.59%
1971	260	130	3,263	647	29.13%	5.78%
1972	300	150	3,862	1,401	33.58%	12.19%
1973	300	150	3,903	1,901	33.36%	16.25%
1974	330	165	4,688	3,435	35.51%	26.03%
1975	350	175	5,202	2,887	35.15%	19.50%
1976	380	190	5,571	3,568	35.48%	22.73%
1977	400	200	5,881	2,948	35.01%	17.55%
1978	450	225	6,471	4,104	36.98%	23.45%
1979	473	237	6,728	4,248	35.22%	22.24%
1980	513	257	7,362	5,527	34.73%	26.07%
1981	561	281	8,113	6,764	34.67%	28.91%
1982	590	295	8,784	7,587	35.14%	30.35%
1983	619	310	8,413	6,527	31.99%	24.82%
34	675	338	9,246	5,764	33.26%	20.73%
1985	763	382	9,925	4,166	34.93%	14.66%

SOURCE: See Appendix II

Appendix IIIb

Housing Costs, 1968-85, Region: Midwest (Recent Purchasers)

Year	House Value (median)	After Tax Mortgage Payment	After Tax Property Tax	Utility Payment	Household Income (median)	Tax Savings	Appreciation	Equity	Opportunity Cost of Equity
1968	17,500	751	247	550	8,700	91	167	6,245	288
1969	18,000	807	251	550	9,380	125	500	6,228	356
1970	19,000	947	257	550	10,000	160	833	5,587	370
1971	20,000	1,130	280	450	10,500	103	1,167	4,490	174
1972	21,500	1,342	338	470	11,000	58	1,333	3,937	156
1973	23,000	1,410	306	490	11,700	78	1,667	4,287	249
1974	25,000	1,659	350	570	13,200	175	1,833	4,908	417
1975	27,000	1,916	378	640	14,000	103	2,333	5,470	271
1976	30,000	2,058	402	700	15,000	112	3,333	6,287	272
1977	35,000	2,357	430	800	16,700	125	4,333	7,744	342
1978	40,000	2,754	441	900	17,500	244	5,000	11,185	671
1979	45,000	2,859	464	960	18,900	259	4,333	15,977	1,199
1980	48,000	3,028	482	1,140	19,800	348	3,533	21,006	1,739
1981	50,000	3,459	505	1,200	21,500	331	2,100	23,322	2,314
1982	51,500	3,701	515	1,320	22,700	616	1,500	24,537	2,064
1983	52,500	4,048	568	1,390	24,300	427	800	25,861	1,617
1984	53,000	4,267	574	1,450	25,340	510	1,133	25,655	1,810
1985	54,700	4,161	591	1,474	25,897	492	1,300	22,756	1,476

Housing Costs, 1968-85, Region: Midwest (Recent Purchasers)

Year	Maintenance & Repairs	Insurance	After Tax Cash Costs of Ownership	= Total Costs of Ownership	Cash Costs Burden	Total Costs Burden
1968	175	88	1,999	2,120	22.82%	24.20%
1969	180	90	2,097	1,954	22.36%	20.83%
1970	190	95	2,203	1,740	22.03%	17.40%
1971	200	100	2,526	1,533	24.52%	14.88%
1972	215	108	2,875	1,698	26.14%	15.44%
1973	230	115	2,988	1,570	25.54%	13.42%
1974	250	125	3,517	2,001	26.65%	15.16%
1975	270	135	3,969	1,907	28.35%	13.62%
1976	300	150	4,310	1,249	28.73%	8.33%
1977	350	175	4,939	948	29.57%	5.67%
1978	400	200	5,609	1,280	32.42%	7.31%
1979	450	225	6,008	2,874	31.79%	15.20%
1980	480	240	6,491	4,696	32.78%	23.72%
1981	506	253	7,102	7,315	33.03%	34.02%
1982	513	257	7,502	8,066	33.05%	35.53%
1983	525	263	7,019	7,835	28.88%	32.24%
1984	530	265	7,323	8,000	28.90%	31.57%
1985	547	274	7,324	7,500	28.28%	28.96%

SOURCE: See Appendix II

Appendix IIIc

Housing Costs, 1968-85, Region: South (Recent Purchasers)

Year	House Value (median)	After Tax Mortgage payment	After Tax Property tax	Utility payment	Household Income (median)	Tax Savings	Appreciation	Equity	Opportunity Cost of Equity
1968	12,000	547	100	250	7,200	1	333	4,200	196
1969	13,000	629	101	250	7,700	25	1,000	4,300	252
1970	15,000	793	102	350	8,200	67	1,267	4,500	258
1971	15,800	957	120	350	8,500	0	1,500	4,266	171
1972	17,500	1,130	130	370	9,100	0	1,000	3,523	142
1973	18,000	1,153	150	390	9,800	0	1,400	3,123	185
1974	20,000	1,401	157	500	11,100	27	2,500	3,417	225
1975	25,000	1,854	160	640	11,800	1	2,067	4,100	206
1976	26,000	1,865	170	700	12,700	0	3,333	4,720	207
1977	30,000	2,111	190	700	13,800	0	3,333	5,520	249
1978	35,000	2,516	186	840	14,900	65	4,567	6,703	410
1979	39,700	2,654	195	900	16,200	69	4,567	9,780	753
1980	43,700	2,887	191	1,080	17,000	153	3,933	14,280	1,221
1981	46,800	3,334	202	1,100	19,400	312	3,233	19,085	1,956
1982	49,400	3,677	225	1,250	20,000	432	2,800	21,763	1,879
1983	52,100	3,135	250	1,320	21,700	267	2,300	23,572	1,659
1984	53,700	3,419	273	1,380	22,800	358	2,433	23,002	1,877
1985	56,700	3,377	288	1,402	23,302	358	2,533	23,966	1,616

Housing Costs, 1968-85, Region: South (Recent Purchasers)

Year	Maintenance & Repairs	Insurance	After Tax Cash Costs of Ownership	Total Costs of Ownership	Cash Costs Burden	Total Costs Burden
1968	120	60	1,357	1,220	18.85%	16.94%
1969	130	65	1,479	731	19.20%	9.49%
1970	150	75	1,821	812	22.20%	9.90%
1971	158	79	2,033	703	23.91%	8.27%
1972	175	88	2,301	1,443	25.29%	15.86%
1973	180	90	2,383	1,168	24.32%	11.92%
1974	200	100	2,884	609	25.99%	5.49%
1975	250	125	3,613	1,152	30.61%	9.76%
1976	260	130	3,732	605	29.38%	4.77%
1977	300	150	4,211	1,126	30.51%	8.16%
1978	350	175	4,883	726	32.77%	4.87%
1979	397	199	5,272	1,458	32.54%	9.00%
1980	437	219	5,833	3,120	33.14%	17.73%
1981	468	234	6,430	5,153	33.15%	26.56%
1982	494	247	7,046	6,125	34.20%	29.73%
1983	521	261	6,702	6,062	30.89%	27.93%
1984	537	269	7,130	6,574	31.27%	28.83%
1985	567	284	7,241	6,324	31.07%	27.14%

SOURCE: See Appendix II.

Appendix III-d

Housing Costs: 1968-85; Region: West (Recent Purchasers)

Year	House Value (median)	After-Tax Mortgage Payment	After-Tax Property Tax	Utility Payments	Household Income (median)	Tax Savings	Capital Gains	Equity	Opportunity Cost of Equity
1968	18,000	740	270	250	9,300	114	1,000	11,300	267
1969	20,000	870	290	330	10,000	102	833	12,000	173
1970	20,000	981	293	350	10,700	202	1,167	13,013	366
1971	21,500	1,186	327	350	11,000	147	1,467	13,018	336
1972	25,000	1,314	384	305	11,800	136	2,333	4,805	380
1973	27,000	1,503	424	387	12,700	175	2,833	4,472	258
1974	30,000	1,905	428	401	14,100	284	2,667	5,667	529
1975	35,000	2,240	403	500	15,200	345	4,333	5,880	398
1976	40,000	2,904	499	504	16,300	310	6,000	6,900	296
1977	48,000	3,660	586	600	17,800	309	9,000	8,500	508
1978	60,000	3,850	470	648	18,900	537	3,033	10,020	667
1979	68,900	4,102	420	720	20,500	680	9,500	10,018	1,251
1980	77,700	4,558	451	830	22,700	806	7,033	23,012	2,049
1981	83,800	5,304	425	936	24,900	1,288	9,700	33,820	3,240
1982	86,000	5,708	442	1,010	25,700	1,511	3,800	38,940	3,112
1983	89,100	4,734	472	1,060	28,000	1,080	2,033	41,148	2,716
1984	89,900	5,149	476	1,110	29,300	1,234	1,167	40,520	3,000
1985	89,500	4,818	476	1,128	30,149	1,134	333	39,480	2,508

Housing Costs: 1968-85; Region: West (Recent Purchasers)

Year	Maintenance & Repairs	Insurance	After-Tax Cash Costs of Ownership	Total Costs of Ownership	Cash Costs Burden	Total Costs Burden
1968	180	90	1,959	1,246	21.06%	13.40%
1969	200	100	2,280	1,827	22.80%	18.27%
1970	200	100	2,391	1,591	22.35%	14.87%
1971	215	108	2,710	1,279	24.64%	11.63%
1972	250	125	3,222	1,078	27.30%	9.14%
1973	270	135	3,439	864	27.08%	6.80%
1974	300	150	3,974	1,633	28.19%	11.58%
1975	330	165	4,524	479	29.76%	3.15%
1976	400	200	5,201	503	31.91%	3.08%
1977	480	240	6,072	2,565	34.11%	14.40%
1978	600	300	7,277	1,709	38.51%	9.04%
1979	680	345	7,890	779	38.49%	3.80%
1980	777	389	8,798	2,907	38.76%	12.81%
1981	838	419	9,877	7,443	39.67%	29.89%
1982	860	430	10,456	9,768	39.16%	36.58%
1983	891	446	9,741	10,424	34.79%	37.23%
1984	899	450	10,181	12,020	34.51%	40.75%
1985	895	448	9,853	12,227	32.68%	40.56%

SOURCE: See Appendix II.

Appendix IV

U.S. Housing Costs 1968-1985, All Households (non mover, owner-occupied)

Year	House Value (median)	After Tax Mortgage payment	After Tax Property tax	Utility payment	Household Income (median)	Insufficient Deductions	Tax Savings	Appreciation	Equity	Opportunity Cost of Equity
1968	16,500	487	248	350	8,500	575	35	833	10,500	484
1969	18,000	549	251	350	9,100	545	60	667	10,833	620
1970	18,000	646	240	350	9,700	515	88	1,167	11,000	615
1971	20,000	811	294	350	10,000	1,000	25	1,333	12,167	478
1972	22,000	860	320	370	10,700	1,465	0	2,333	13,167	522
1973	25,000	940	360	390	11,500	1,425	0	2,000	15,500	901
1974	26,000	1,032	367	590	12,800	1,300	11	2,500	16,750	1,082
1975	29,500	1,120	380	600	13,600	1,920	0	2,500	19,083	947
1976	32,500	1,290	410	720	14,500	2,075	0	3,667	21,417	885
1977	37,000	1,400	400	800	16,000	2,400	0	4,167	23,667	1,054
1978	42,000	1,570	450	870	16,800	2,360	0	4,867	26,500	1,600
1979	47,100	1,660	450	950	18,300	2,485	0	4,767	30,833	2,315
1980	51,300	1,800	400	1,120	19,800	2,410	0	4,433	33,333	2,759
1981	55,300	1,907	494	1,170	21,800	2,510	29	3,300	36,333	3,605
1982	57,000	2,014	520	1,320	23,200	2,240	96	2,800	38,667	3,232
1983	59,700	2,034	544	1,390	24,400	2,180	122	2,067	42,000	2,827
1984	61,500	2,078	557	1,450	25,700	2,115	155	2,367	45,733	3,500
1985	64,100	2,061	579	1,473	26,265	2,087	165	2,333	49,333	3,202

Housing Costs, 1968-85, All Households

Year	Maintenance & Repairs	Insurance	After Tax Cash Costs of Ownership	Total Costs of Ownership	Cash Costs Burden	Total Costs Burden
1968	165	83	1,332	983	15.68%	11.56%
1969	180	90	1,420	1,373	15.61%	15.09%
1970	180	90	1,512	960	15.58%	9.89%
1971	200	100	1,755	899	17.55%	8.99%
1972	220	110	1,880	69	17.57%	0.65%
1973	250	125	2,065	966	17.96%	8.40%
1974	260	130	2,380	962	18.59%	7.51%
1975	295	148	2,603	1,049	19.14%	7.72%
1976	325	163	2,908	126	20.05%	0.87%
1977	370	185	3,215	102	20.09%	0.64%
1978	420	210	3,520	253	20.95%	1.51%
1979	471	236	3,767	1,315	20.58%	7.18%
1980	513	257	4,150	2,475	20.96%	12.50%
1981	553	277	4,400	4,705	20.18%	21.58%
1982	570	285	4,709	5,141	20.30%	22.16%
1983	597	299	4,863	5,624	19.93%	23.05%
84	615	308	5,007	6,141	19.48%	23.89%
1985	641	321	5,075	5,944	19.32%	22.63%

SOURCE: See Appendix II

Appendix Va

Percentage of Households that Rent, 1974-83

CATEGORY	1974	1980	1983
All Households	35.40	34.58	35.32
Household Type			
1 Male Single Adult	68.55	61.60	59.74
2 Female Single Adult	51.06	51.02	49.04
3 Unrelated Adults	47.58	50.67	50.28
4 Married Couple Alone	20.80	20.06	20.54
5 Married Couple, Other Rels., No Children	23.73	22.24	22.45
6 Married Couple, Oldest Child < 6	42.54	39.74	39.05
7 Married Couple, Oldest Child 6-17	18.45	17.27	20.54
8 Married Couple, Children, Other Rels	25.10	20.84	31.06
9 Male Single Parent	51.74	42.55	45.05
10 Female Single Parent, Oldest Child < 6	86.89	88.60	88.56
11 Female Single Parent, Oldest Child 6-17	59.16	60.19	62.50
12 Female Single Parent, Other Rels.	58.78	65.96	66.32
Age Bracket (for Household Head)			
1 < 25	77.36	78.72	80.05
2 25-34	48.11	47.70	51.81
3 35-44	28.50	27.06	30.82
4 45-64	23.86	21.56	22.11
5 >= 65	30.22	27.67	20.42
Household Income Class			
1 Lowest	51.57	52.16	54.66
2 Second	36.44	36.72	37.00
3 Third	29.50	29.04	29.94
4 Highest	24.70	19.92	20.82

SOURCE: Authors' tabulations, based on U.S. Department of Housing and Urban Development, *Annual Housing Survey* tapes, various years.

Appendix Vb

Percentage Distribution of Renter Households, 1974-83

CATEGORY	1974	1980	1983
All Renter Households	100.00	100.00	100.00
Household Type			
1. Male Single Adult	13.57	15.00	14.78
2. Female Single Adult	17.78	19.70	18.32
3. Unrelated Adults	9.03	13.49	13.87
4. Married Couple Alone	21.31	16.86	16.53
5. Married Couple: Other Rels./No Children	1.72	1.72	1.87
6. Married Couple: Oldest Child < 6	10.48	8.13	8.70
7. Married Couple: Oldest Child 6-17	13.07	11.01	11.01
8. Married Couple: Children/Other Rels.	1.49	1.75	1.82
9. Male Single Parent	1.03	0.94	1.00
10. Female Single Parent: Oldest Child < 6	2.27	2.42	2.30
11. Female Single Parent: Oldest Child 6-17	0.40	0.95	0.90
12. Female Single Parent: Other Rels.	1.14	1.00	1.09
Age Bracket (for Household Head)			
1. < 25	18.07	17.60	15.13
2. 25-34	27.88	32.31	33.27
3. 35-44	13.70	14.08	17.00
4. 45-64	23.18	19.54	18.88
5. >= 65	16.57	16.30	15.72
Household Income Class			
1. Lowest	35.00	39.70	39.70
2. Second	24.74	25.08	23.33
3. Third	21.12	20.09	19.32
4. Highest	18.54	15.02	17.56

SOURCE: Authors' tabulations. Based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various years.

Appendix Vc

Decomposing the Change in the Number of Renter Households, 1974-83

	% Change 1974-80			% Change 1980-83			% Change 1974-83		
CATEGORY	Total Households	% Renters	Renter Households	Total Households	% Renters	Renter Households	Total Households	% Renters	Renter Households
Renters	21.5%	-2.0%	19.0%	[illegible]	-2.7%	8.0%	28.4%	18.5%	28.1%
Household Type									
1	47.0%	-9.7%	34.2%	9.0%	3.2%	6.4%	62.1%	12.0%	41.7%
2	30.8%	-0.1%	30.7%	8.0%	-5.9%	1.0%	37.8%	4.0%	32.0%
3	70.5%	0.5%	60.5%	12.5%	0.9%	11.0%	89.8%	8.7%	78.0%
4	18.8%	-21.4%	-6.6%	7.2%	11.7%	6.5%	27.3%	21.0%	0.0%
5	20.2%	-6.3%	18.5%	10.7%	1.0%	17.8%	37.8%	8.4%	33.4%
6	8.7%	-13.2%	-8.2%	0.0%	6.7%	18.0%	12.7%	9.6%	16.5%
7	10.0%	-6.5%	-10.6%	3.1%	16.8%	17.1%	3.9%	11.4%	16.8%
8	29.9%	6.7%	38.0%	8.0%	16.9%	12.0%	25.2%	24.7%	36.1%
9	30.5%	-17.8%	7.8%	14.2%	1.2%	15.0%	49.1%	10.8%	24.0%
10	24.5%	2.0%	25.0%	9.2%	0.0%	9.2%	27.8%	3.1%	25.0%
11	25.9%	1.7%	28.1%	5.4%	1.9%	7.8%	30.7%	8.7%	38.3%
12	76.0%	11.2%	80.7%	12.1%	1.3%	21.8%	96.4%	12.8%	121.8%
Age Bracket									
< 25	8.7%	1.7%	10.0%	-0.4%	1.9%	7.2%	11.8%	4.2%	2.7%
25-34	30.2%	0.7%	31.1%	6.1%	6.5%	11.8%	41.6%	7.7%	81.2%
35-44	23.0%	-2.9%	20.0%	27.7%	33.4%	31.1%	48.4%	8.2%	57.4%
45-64	8.8%	0.0%	11.5%	2.4%	2.5%	5.0%	11.4%	7.1%	9.2%
>= 65	20.0%	-8.4%	15.3%	9.8%	4.3%	4.2%	33.8%	12.0%	20.2%
Income Class									
Lowest	11.0%	4.2%	12.1%	3.9%	4.8%	8.5%	15.6%	3.0%	11.8%
Second	14.1%	0.8%	14.9%	-2.4%	0.2%	3.3%	20.8%	4.0%	20.8%
Third	18.1%	-1.0%	16.2%	1.4%	3.1%	1.7%	19.5%	3.2%	17.0%
Highest	23.9%	-10.4%	18.5%	10.7%	6.0%	21.5%	33.0%	15.5%	28.9%

SOURCE: Authors' calculations, based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various years.

Note: Household types are defined in Appendix Vb. By definition, the percentage change in renter households equals the percentage change in total households plus the percentage change in the renter share plus the product of the [illegible] two factors [illegible].

Appendix VIa
Percentage Distribution of Rent Burdens, 1974

Category	Gross Rent as Percent of Income			
	< 25%	25-49%	50-74%	>= 75%
All Renter Households	60.65	24.97	6.09	8.29
Household Type				
1. Male Single Adult	66.31	21.86	5.22	6.61
2. Female Single Adult	39.40	37.21	12.59	10.80
3. Unrelated Adults	46.86	32.00	9.77	11.37
4. Married Couple Alone	73.37	18.13	3.03	5.47
5. Married Couple, Other Rels., No Children	68.03	20.80	3.86	7.31
6. Married Couple, Oldest Child < 6	72.87	19.00	2.90	5.23
7. Married Couple, Oldest Child 6-17	73.08	15.69	2.25	8.97
8. Married Couple, Children, Other Rels.	73.24	12.86	4.28	9.62
9. Male Single Parent	62.79	25.06	4.09	7.40
10. Female Single Parent, Child < 6	28.06	34.09	21.16	16.69
11. Female Single Parent, Child 6-17	39.51	37.08	14.78	8.64
12. Female Single Parent, Other Rels.	38.80	33.97	16.69	10.54
Age Bracket (for Household Head)				
1. <= 24	54.01	27.30	8.71	9.98
2. 25-34	68.04	21.67	4.71	5.59
3. 35-44	67.59	19.51	4.09	8.41
4. 45-64	62.56	22.65	6.79	8.00
5. >= 65	42.89	35.64	11.45	10.02
Household Income Class				
1. Lowest	30.09	35.08	18.14	16.69
2. Second	59.52	37.45	2.75	0.27
3. Third	84.44	15.29	0.18	0.09
4. Highest	96.49	3.47	0.01	0.03

SOURCE: Authors' tabulations, based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various issues.

Appendix VIb

Percentage Distribution of Rent Burdens, 1980

CATEGORY	Gross Rent as Percent of Income			
	< 25%	25-49%	50-74%	>= 75%
All Renter Households	50.31	29.55	9.13	11.01
Household Type				
1. Male Single Adult	58.62	26.64	6.08	8.66
2. Female Single Adult	57.71	17.36	13.24	11.69
3. Unrelated Adults	40.01	32.57	11.48	15.95
4. Married Couple Alone	65.08	22.69	4.61	7.62
5. Married Couple, Other Rels., No Child	59.69	22.61	6.36	11.34
6. Married Couple, Oldest Child < 6	58.48	29.28	4.79	7.45
7. Married Couple, Oldest Child 6-17	61.55	23.41	5.14	9.91
8. Married Couple, Children + Other Rels.	59.35	24.51	5.49	10.66
9. Male Single Parent	52.58	29.93	9.62	7.87
10. Female Single Parent, Child < 6	24.11	28.92	20.30	26.67
11. Female Single Parent, Child 6-17	31.24	38.41	17.00	13.35
12. Female Single Parent, Other Rels.	36.65	31.83	13.87	17.65
Age Bracket (for Household Head)				
1. < = 24	41.57	32.08	11.16	15.18
2. 25-34	55.49	28.42	7.05	9.04
3. 35-44	55.10	27.86	7.18	9.87
4. 45-64	54.88	25.00	8.65	11.24
5. > = 65	40.34	35.22	13.34	11.10
Household Income Class				
1. Lowest	25.81	32.32	20.07	21.80
2. Second	45.99	48.06	5.16	0.79
3. Third	74.23	24.81	0.89	0.07
4. Highest	94.63	5.33	0.04	0.00

SOURCE: Authors' tabulations based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various years.

Appendix VIc

Percentage Distribution of Rent Burdens, 1983

CATEGORY	Gross Rent as Percent of Income			
	< 25%	25-49%	50-74%	> = 75%
All Renter Households	45.76	31.43	9.94	12.87
Household Type				
1. Male Single Adult	54.55	28.03	7.69	9.74
2. Female Single Adult	36.51	37.31	12.98	13.20
3. Unrelated Adults	34.34	35.90	12.72	17.05
4. Married Couple Alone	62.25	25.40	5.11	7.24
5. Married Couple, Other Rels., No Child	53.04	25.47	6.16	15.32
6. Married Couple, Oldest Child < 6	51.66	31.05	7.57	9.72
7. Married Couple, Oldest Child 6-17	53.68	28.04	6.57	11.71
8. Married Couple, Children, Other Rels.	50.02	34.74	6.91	8.33
9. Male Single Parent	48.36	29.15	11.71	10.78
10. Female Single Parent, Child < 6	17.37	27.50	20.58	34.55
11. Female Single Parent, Child 6-17	25.70	37.15	17.29	19.86
12. Female Single Parent, Other Rels.	25.60	31.66	17.83	24.91
Age Bracket (for Household Head)				
1. < = 24	34.96	32.03	13.86	19.15
2. 25-34	49.44	30.42	8.80	11.34
3. 35-44	50.90	29.40	8.18	11.51
4. 45-64	50.45	28.30	8.17	13.08
5. > = 65	37.20	38.94	12.62	11.24
Household Income Class				
1. Lowest	20.92	31.75	20.53	26.80
2. Second	40.76	50.73	7.69	0.82
3. Third	66.80	32.07	1.04	0.03
4. Highest	90.85	8.78	0.32	0.05

SOURCE: Authors' tabulations, based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various years.

Appendix VII

Renter Households with Inadequate Housing, 1974 and 1983

CATEGORY	% of Renters 1974	% of Renters 1983	Number of Renters 1974	Number of Renters 1983
All Renter Households	15.5%	12.8%	3,603,065	3,840,038
Household Type				
1. Male Single Adult	10.9%	13.1%	622,747	580,930
2. Female Single Adult	11.8%	9.1%	491,783	500,744
3. Unrelated Adults	15.7%	11.9%	364,968	496,262
4. Married Couple Alone	11.9%	10.6%	591,893	525,334
5. Married Couple, Rels., No Child	23.8%	15.1%	95,587	90,069
6. Married Couple, Oldest Child < 6	12.9%	13.9%	316,476	361,445
7. Married Couple, Child 6-17	18.5%	15.4%	565,062	548,727
8. Married Couple, Children, Rels.	29.3%	20.8%	102,144	115,356
9. Male Single Parent	18.1%	14.7%	22,656	45,941
10. Female Single Parent, Child < 6	15.1%	17.8%	79,855	122,046
11. Female Single Parent, Child 6-17	18.1%	15.4%	271,093	317,409
12. Female Single Parent, Rels.	29.0%	24.3%	78,821	145,135
Age Bracket (for Household Head)				
1. < = 25	12.5%	12.5%	339,461	565,354
2. 25-34	15.4%	13.1%	870,571	1,301,590
3. 35-44	18.2%	13.2%	580,376	670,143
4. 45-64	18.5%	14.2%	993,035	802,048
5. > = 65	15.8%	10.8%	612,722	506,913
Household Income Class				
1. Lowest	22.1%	18.1%	1,828,106	2,162,262
2. Second	15.4%	13.6%	887,265	653,554
3. Third	10.7%	10.2%	529,133	588,068
4. Highest	8.4%	10.2%	361,541	538,985

SOURCE: Authors' tabulations based on U.S. Department of Housing and Urban Development, Annual Housing Survey tapes, various years.

Senator Cranston. Thank you very much for your very helpful testimony and for your brevity, as well as the substance that you gave to us. Mr. McMillan.

STATEMENT OF ROBERT R. McMILLAN, ESQUIRE, CHAIRMAN, LONG ISLAND ASSOCIATION'S COMMITTEE ON HOUSING, UNIONDALE, NY

Mr. McMillan. Mr. Chairman, Senator D'Amato, fellow Long Islander.

My name is Robert McMillan. I am partner in the law firm of Rivkin, Radler, Dunne & Bayh and chairman of the Long Island Association's Housing Committee. The Long Island Association is one of the largest business organizations in the region with more than 3,000 members, employing 400,000 people in Nassau and Suffolk Counties of New York State. Our members include several very large companies, such as Grumman, Tambrands, Hazeltine, Hartman Systems, and Unisys. We also represent many banks, small businesses with as few as two or three employees and our membership includes all area colleges and universities.

In April 1986, a new standing committee on housing was added to the LIA's structure. The committee was charged with the responsibility of presenting recommendations on what steps should be taken to deal with the region's growing "entry level" or "affordable housing" dilemma.

I would like to submit a copy of our report for the record.

Next I would like to address the reasons which caused a major regional business group to put so much time and energy into the issue of housing. The answer is very simple. Demands for more membership caused the action. Long Island has had tremendous economic growth over the last decade. In fact, the number of jobs in Nassau and Suffolk has more than doubled in the last 10 years and now stands at close to 1 million. The economic growth and the fact that almost 80 percent of Long Island families live in owner-occupied homes has driven the price of housing at an unprecedented rate. The result is the lack of housing for young families starting out, our children, our senior citizens desiring to scale down, new employees attracted to the Island for expanding job opportunities.

In just the last 6 years, the median price of a home has more than doubled from $63,000 to over $160,000. Most of the increase is directly attributable to land costs.

During the same period the median family income rose from $29,000 to approximately $43,000. While our median family income is the highest in the Nation, the median home is completely out of reach for the median family, unless there is a family subsidy. Rental units are almost nonexistent.

Long Island businesses are faced every day with refusals from perspective employees, not because of a lack of culture, parks, beaches, golf courses or educational facilities, but because those employees interested in the new job opportunity, come to Long Island to look for housing and realize they cannot secure an adequate place to live.

Several Long Island businesses, out of desperation, have resorted to the costly private busing of employees from New York City to fill gaps in employment.

Not only does the lack of affordable housing impact perspective employees, but current employees are often lured away because a better life style, in terms of housing, is available with employment off of the Island.

There are other dimensions, as well. In planning for future expansion, the impact of housing costs has caused more and more Long Island businesses to expand elsewhere. This puts directly at risk our future economic development.

Second, there are companies which come to Long Island looking for a new office or a plant site and decide not to locate on the Island because of the housing factor.

Our report covers some suggestions which may be useful from the Federal level. I would also urge you to consider donation of Federal lands to not-for-profit affordable housing organizations. Nassau and Suffolk Counties, as well as the State of New York, use such an approach in cooperation with local governments.

In closing, I would like to comment on one of the other key deterrents to the development of affordable housing and probably elsewhere. That is public attitudes. Local government is often paralyzed because of community opposition to any form of affordable housing. By failing to act on affordable housing, we also may very well be killing future economic growth on Long Island. That growth has fueled the dramatic price increases. If the economic growth slows or declines, that will soon negatively impact on current home values, values which are so jealously guarded by my fellow Long Islanders in what I believe is their misplaced opposition to entry level housing.

Thank you, Mr. Chairman.

[The complete prepared statement of Robert R. McMillan follows:]

Remarks of Robert R. McMillan, Chairman of the Long Island Association's Committee on Housing Before the United States Senate Subcommittee on Housing, Washington, D.C. --- July 1, 1987

Mr. Chairman, my name is Robert R. McMillan. I am a partner in the law firm of Rivkin, Radler, Dunne & Bayh and Chairman of the Long Island Association's Housing Committee. The Long Island Association (LIA) is one of the largest business organizations in the region with more than 3,000 members employing 400,000 people in Nassau and Suffolk counties of New York State. Our members include several very large companies such as Grumman, Tambrands, Hazeltine, Hartman Systems and Unisys. We also represent many small businesses with as few as two or three employees and our membership includes all area colleges and universities.

In April of 1986, a new standing committee on housing was added to the LIA's structure. The committee was charged with the responsibility of presenting recommendations to the Board of the LIA on what steps should be taken to deal with the region's growing "entry level" or "affordable housing" dilemma. The committee completed its preliminary work earlier this year, and our committee's recommendations were endorsed unanimously by the Board of the LIA. I would like to submit a copy of that report for the record.

Next, I would like to address the reasons which caused a major regional business organization to put so much time and energy into the issue of housing. The answer is very simple. Demands from our membership caused the action. Long Island has had tremendous economic growth over the last decade. In fact, the number of jobs in Nassau and Suffolk has more than doubled in the last ten years and stands at close to one million.

The economic growth and the fact that almost eighty percent of Long Island families live in owner occupied homes has driven the price of housing at an unprecedented rate. The result is a lack of housing for young families starting out; our senior citizens desiring to scale down; and new employees attracted to the Island for expanding job opportunities.

In just the last six years the median price of a home has more than doubled -- from $63,000 to about $160,000. (Most of the increase is directly attributed to land costs.) During the same period, the median family income rose from around $29,000 to approximately $43,000. While our median family income is the highest in the nation, the "median home" is completely out of reach for the "median family" unless there is a family subsidy. Rental units are almost nonexistent. The facts are that the young (our children), senior citizens and new employees are priced out of the Long Island market.

Long Island businesses are faced every day with refusals from prospective employees -- not because of a lack of culture, parks, beaches, golf courses or educational facilities -- but because those employees interested in the new job opportunity come to Long Island to look for housing and realize they cannot secure an adequate place to live. Several Long Island businesses, out of desperation, have resorted to the costly private busing of employees from New York City to fill gaps in employment. Not only does the lack of affordable housing impact prospective employees, but current employees are often lured away, because a better life style, in terms of housing, is available with employment off of Long Island.

There are other dimensions to the lack of affordable housing. First, as the price of housing escalates, businesses are forced to raise salaries to remain competitive for engineers, sales personnel and attorneys, to name just a few categories. In planning for future expansion, the impact of housing costs has caused more and more Long Island businesses to expand elsewhere. This puts directly at risk our future economic development.

Second, there are the companies which come to Long Island looking for a new office or plant site and decide not to locate on the Island because of the housing factor. It is clear, in my mind, that the lack of affordable housing contributes to family dislocation and slows economic growth.

While our report, previously submitted for the record, covers some suggestions which may be suitable for use at the federal level, I would also urge you to consider the possible donation of federal lands to not for profit affordable housing organizations. Nassau and Suffolk Counties, as well as the State of New York, use such an approach in cooperation with local governments. The price of land is the key ingredient to affordable housing.

In closing, I would like to comment on one of the key deterrents to the development of affordable housing on Long Island -- public attitudes. Local government is often paralyzed because of community opposition to any form of affordable housing. By failing to act on affordable housing, we also may very well be killing further economic growth on Long Island. That growth has fueled the dramatic price increases. If the economic growth slows or declines, that will soon negatively impact on current home values -- values which are so jealously guarded by Long Islanders in their misplaced opposition to affordable housing.

LONG ISLAND ASSOCIATION
RECOMMENDATIONS AND ACTIONS ON
AFFORDABLE HOUSING FOR LONG ISLAND

The price of housing on Long Island has reached a point where entry level executives and professionals, our office workers, senior citizens and junior citizens and blue collar workers cannot afford to live on Long Island. The housing crisis which this has precipitated led the Long Island Association Housing Committee to try and determine what actions could be taken by the LIA to rectify this situation.

In response to the affordable housing issue, the Housing Committee recommends that the LIA Board of Directors adopt the following recommendations and actions:

1. The LIA should serve as a catalyst and partner in the development of a comprehensive public relations/educational campaign designed to influence community attitudes regarding the need for affordable housing programs on Long Island.

2. The LIA should encourage local governments, where possible, and where appropriate, to increase the density of projects, either through cluster zoning, two family homes, reductions in lot sizes and square footage requirements, development of rental units or construction of mid-rise projects which will aid in reducing the costs of housing.

3. The LIA should support the availability of affordable housing programs on a local, state and federal basis, specifically the growth of the New York State Affordable Housing Program.

4. The LIA should support and become more active in the political process on a local level to encourage the development of affordable housing programs by muncipalities. In addition, individual businesses must become more aware of the local political process and its effect on the affordable housing issue.

5. The LIA should continue its investigation into the feasibility of forming a private development corporation to help in the development of affordable housing projects.

6. The LIA should encourage, with proper safeguards for safety and health, two-family homes and rental units so as to provide alternatives to the single family home.

7. The LIA should bring together developers, attorneys, financial institutions, architects, government officials and housing advocates to design and implement programs to lower the cost of housing projects.

8. The LIA must encourage town and village officials to incorporate affordable housing into their master plans so as to provide a legal basis for the construction of such housing. State assistance should be requested to help pay for the development of such programs, which must include affordable housing development.

9. The LIA should continue to support a constitutional amendment to provide counties with specific housing powers.

10. The LIA should encourage municipalities to accelerate the processing of applications and the granting of permits for affordable housing projects.

Long Island's housing market has reached a crossroads which may decide whether the economic well-being of Long Island will continue. While a few years ago the housing issue on Long Island concerned itself with the spectre of boarded up houses, reductions in housing values and businesses moving off Long Island, today our housing market is faced with the transformation of our communities into havens of $300,000 to $1 million homes, which can only be purchased by fewer and fewer Long Islanders. While the value of our homes has skyrocketed, our housing values may have declined, to the point where a realization has occurred that the housing issue is not just for the poor, but now plays a major role in the decisions made every day by the business leaders of Long Island.

For many years, most people have not given a second thought to housing having any effect in the business decisions of Long Island. The Long Island economy is booming, housing values continue to increase far beyond the inflationary index and Long Island maintains its attractiveness as a single-family home community. However, as housing prices have continued to escalate, it has become clear that it is becoming more and more difficult for those trying to enter the Long Island job market or those being transfered into Long Island to find housing on Long Island which they could afford. With the average purchase price of a home on Long Island reaching $155,000 and new home average prices reaching $210,000 in Nassau County, most blue and white collar workers find themselves almost completely priced out of the market. Companies cannot transfer employees onto Long Island without significantly subsidizing the housing cost differentials between their homes in other parts of the country and what is available on Long Island. New employees, faced with competing salaries, often choose to locate off of Long Island because they do not want or cannot afford the significantly higher Long Island housing costs. Long Island companies find themselves unable to compete for the top professionals and engineers, saying nothing about blue collar workers, with other parts of the country, not because of the salary or fringe benefits being offered, but solely because of the cost of housing.

These factors clearly demonstrate the effect that the affordable housing problem is having and will continue to have on the Long Island economy. The future economic success of Long Island may depend in large part on whether the housing issue can be solved. Indications are that the Long Island economy may create 100,000 new jobs between now and the year 2000. Most of these new jobs will be created in the service industry, with salaries of between $20,000 - $30,000. At these pay scales, many new job entrants would find themselves faced with the impossibility of paying between 50-90 percent of their household income on housing. This is far above the usual average of between 20-27 percent of household income being spent on housing costs. Therefore, unable to house them, it will be impossible for Long Island to attract the workers necessary to continue Long Island's expansion and competiveness in an increasingly worldwide economy.

The inability to provide housing for our current workers, let alone the 100,000 new jobs which may be created, may become a driving force in the possible downturn in the economy of Long Island. Long Island business leaders, faced with the inability to attract the required workforce necessary, will turn to other areas of the country where housing costs are not a barrier to the attractiveness of the area.

Faced with these prospects, the Long Island Association, the region's largest business and civic organization, formed the LIA Housing Committee. Its charge was to investigate the affordable housing issue and to recommend to the LIA Board of Directors specific actions the LIA might take to contribute to the favorable resolution of this problem. To determine specific strategies, four sub-committees, each with a separate agenda, were formed. Each sub-committee reviewed materials affecting its part of the affordable housing issue, and developed specific recommendations to encourage the development of additional affordable housing on Long Island.

During the initial discussions of the committee, it became obvious that there existed many different housing issues on Long Island, each playing a role in the continued advancement of both the Long Island economy and its quality of life. Throughout Long Island there are hundreds and thousands of people who face the prospect of being without a place to live each night of the year. The concerns of the poor and homeless are being addressed by a core of not-for-profit organizations and local governments, who are often faced with more and more persons looking for shelter but a declining level of resources with which to take care of them.

In addition, many senior citizens with limited resources are faced with the dilemma of maintaining their homes despite significantly increasing property values and taxes because of an alarming lack of senior citizen housing availability on Long Island. While many organizations and local governments, such as the Diocese of Rockville Centre, are trying to increase the number of senior citizen units available, a lack of resources coupled with community opposition has not yet allowed a significant increase in housing opportunities for our senior citizens to develop.

Instead of duplicating the actions of other organizations whose main thrust is directed at these parts of the housing issue, the Housing Committee decided to concentrate on the affordable housing issue as it relates to business decisions on Long Island. In this regard, it became necessary to first define exactly what "affordable housing" is so that it can be correlated to the job structure of Long Island. State and federal law defines "affordable housing" as housing which can be purchased by individuals with income equal to 80% of the median income of the community being considered. With the median income of Nassau and Suffolk Counties being $34,000, 80% of that became $28,000. This figure, which is the highest in the country for any individual statistical metropolitan area, clearly shows the extent of the problem on Long Island. Taking the usual mortgage requirements in today's marketplace, without a substantial down payment or other subsidy, a couple making $28,000 would only be able to afford a home costing approximately $70,000. With the average home on Long Island costing over $155,000, it is obvious that a dilemma exists for today's prospective homeowners: either pay a much greater percentage of their salary for housing costs (which may be impossible due to the credit requirements of those providing home mortgages) or find a place to live and work off of Long Island. It is this second prospect which may become the unavoidable choice of most entry level job seekers who want to live and work on Long Island, unless something is done soon.

Before the sub-committees could develop specific strategies, certain factors which have played a role in the lack of affordable housing on Long Island were identified. These factors are:

- There are 3 towns, 2 cities and 65 villages in Nassau County and 10 towns and 30 villages in Suffolk County, all with their own local planning board and master plans.

- The shortage of available land significantly increases the price of that land which is available for development.

- Long Island has the highest percentage of single family homes in the country with almost 78% of Long Islanders living in such homes. The single family home is part of our culture and our way of life, and many people feel threatened by multi-family housing.

- The fear of multi-family housing or increased density is exactly why many people moved from New York City to Long Island. The perception remains that multi-family or subsidized housing is only for the poor, even though today it may be the only way to allow the children of Long Islanders, our employees and our senior citizens to continue to live and work on Long Island.

- Zoning restrictions and the time necessary to receive permits from the overlapping governmental agencies exacerbate and showcase the hostility toward multi-family or increased density housing.

Senator CRANSTON. Thank you very much. Ms. Wells.

STATEMENT OF CATHLENE WELLS, PUBLIC SCHOOLTEACHER, LOS ANGELES, CA

Ms. WELLS. Thank you. My name is Cathlene Wells. I teach English at Roosevelt High School in the Los Angeles Unified School District. I am a member of the United Teachers-Los Angeles.

I am here today to talk with you about the severe difficulties currently involved in a teacher being able to purchase a home for him or herself.

I have been a teacher for 18 years. I taught for 16 years in private Catholic institutions. Thirteen years of that time I was a Roman Catholic nun, so received no personal financial reimbursement for my teaching. Soon after I left the convent, my father became chronically ill, and I felt I needed to be in a position to earn more money to help with future medical costs. I have now been teaching in the Los Angeles Unified School District for 2 years.

My yearly gross income, as a second-year teacher, is $22,000. My monthly gross income is $1,973. Three hundred dollars monthly goes to a tax-sheltered annuity toward my retirement, so $1,440 is my net pay. Had I started teaching this year, I would also have a mandatory deduction from my check for Medicare. My rent and gasoline and car upkeep come to $560 a month. Two hundred dollars per month goes toward finishing work on my teaching credential and master's degree. Utilities, insurance, home furnishing payments and a loan payment to cover summer expenses when we do not work, come to approximately $400. One hundred and twenty dollars goes toward food. One hundred and sixty dollars is left for clothing, professional organization dues, professional periodical subscriptions, health needs, emergencies, savings, and recreation.

At this time in my life, I desire very greatly to purchase a home. I would like to live closer to where I teach, so I would not have a 45-minute drive, in traffic, both to and from school. I would like my monthly payments of rent to go toward something of my own rather than to a landlord. For my financial security, I think it is only prudent to invest in a home.

With my tax-sheltered annuity, I have managed to save $3,000 over a period of 2 years. In order to put the 10 percent down on a $100,000 home, which is the lowest price I have found for a condominium in a decent and safe neighborhood, I would have to have $10,000 saved, not including closing costs of approximately $4,000. This would take, at the very least, 5 years to save. This is not taking into consideration that my rent may be raised and my 1975 Chevy Malibu Classic, with over 150,000 miles on it, will need to be replaced within that time.

The cost of living and interest rates will go up during that time also. I am not even taking into account medical or other emergencies that might arise.

Also, most lending agencies prefer 20 percent down. Some agencies will only lend on a single-family dwelling.

I would need to buy something similar to a duplex, since I could not make the $800 to $900 monthly house payments on my salary alone. I would need to have a renter.

Another problem with duplexes or renting situations is that often the renter is not reliable or does not take good care of the property. This adds an extra stress and burden for the teacher who should and needs to be able to spend his or her time planning, evaluating and replanning for the needs of the students. Many of our students are becoming increasingly difficult to reach in a teaching situation because of their very troubled family, economic and personal situations. This requires great creativity and skill on the part of the teacher. Those of us who love teaching, love to do this planning and are energized by it, but it is extremely time-consuming.

Dealing with an unreliable or unsavory renter would take away precious time that is needed to prepare for the student.

In addition, it is very difficult to find a home between $100,000 and $130,000 in an area of the city where there is a pride in the way homes are cared for and where a female teacher would feel safe. It is truly impossible for a single female teacher to have any hope of purchasing a home for at least 5 to 10 years after beginning her teaching. This includes living extremely frugally with very little possibility of money for either relaxation or enrichment, both of which are necessary for all teachers, especially the young who are just beginning.

As I speak, I wonder what person would seriously consider a teaching career now. Could a young man plan to support a family this way? Could a young woman provide for her financial security? Would either one of them want to sacrifice a modest amount of gracious living manifested in their living accommodations, clothing, transportation and recreation while they are saving for a home? Should they be required to? Could a young couple even think of raising a family in this situation?

I have taught for 18 years. I love teaching and do it well. In all honesty, I must say I cannot encourage my high school students to join the teaching profession. Most of them do not even consider it because of the difficulties I have described. Our country needs to attract the idealistic, the talented, even the ambitious, to the teaching profession.

I must sadly say, in closing, that I, too, am considering taking my teaching skills and experience to another field which will pay more. I am 40 years old. I need to take care of myself, so I will be able to give effectively wherever I am. I desire greatly and think it is prudent to have the financial investment of a home.

I believe we need dedicated teachers for our country's future. I believe education is the key to any society's future. But I do not see how I can teach in our public school system, take care of my money and myself wisely, and take care of my parents as they grow older and ill. I feel we are in a depressing and almost hopeless situation regarding teachers being able to buy their own homes. I think it is an urgent issue to address if we want to attract young, talented teachers to this profession.

I am grateful that this committee is considering this serious need, and I believe it is frighteningly true that we teachers, our country's youth, and our country's solidly founded future, are dependent upon your deliberations in this matter.

[This complete prepared statement of Cathlene Wells follows:]

Senator **Cranston**. Thank you very much. I appreciate your coming all the way across the country to share your personal views with us and your description of your budget is, I think, very, very helpful to us.

Ms. **Wells**. Thank you.

Senator **Cranston**. We not only have a terrible problem of housing costing too much, but teachers being paid too little. We have to remedy that.

I want to thank the United Teachers of Los Angeles for sponsoring your appearance here today. Your testimony indicates that the high cost of housing in Los Angeles and other cities and counties is a strong deterrent to recruiting bright and creative individuals to the teaching profession.

I would like to just ask you a few questions. What is the starting salary for teachers in the L.A. School System?

Ms. **Wells**. Our starting salary now is $22,395.

Senator **Cranston**. Given that salary, what are the realistic options for housing for starting teachers?

Ms. **Wells**. Most teachers live in apartments. Some have houses, but they need to live quite a distance from the school, in order to be in a place where they can afford housing.

Senator **Cranston**. What is the average commute, do you think, for teachers in your school?

Ms. **Wells**. Some teachers come from as far as an hour's distance one way. The average would be 35 to 40 minutes, one way.

Senator **Cranston**. Given the absence of nearby affordable housing, has teacher morale been adversely affected?

Ms. **Wells**. Yes. I really think so. Many teachers have given up the hope of ever being able to afford a home and that feeling of hopelessness does affect the enthusiasm and the energy with which they teach.

Senator **Cranston**. You said you are considering other job options. Is that a pretty widespread feeling among teachers now?

Ms. **Wells**. I would say it is a common feeling. It is a common feeling, especially among the new teachers. Several new teachers between 1 to 3 years do make a change in their profession because of these kinds of problems.

Senator **Cranston**. I thank you very, very much.

Ms. **Wells**. Thank you very much.

Senator **Cranston**. Mr. McMillan, in your testimony, you recommended the Federal Government donate Federal lands to nonprofit organizations to help ease the affordable housing problem. Since the high cost of land is one of the major factors, that obviously would be a very fine way to go, if there is appropriate land available where needed.

Do you have any survey or any indication as to how much of that sort of land might be available in communities where housing needs are great?

Mr. **McMillan**. We have no survey, but I am sure that the various departments—Interior, Defense, GSA—probably would be able to come up with where such properties are available. I know that on Long Island, there are some Federal lands that I believe would be suitable. There are others that would be very controversial. I think beyond the land, the other aspect that is important, I believe, would be to help local governments with the infrastructure. Roads, sewers, curbs, sidewalks, I believe, are an area that could be helpful in terms of reducing the price. Interest rates. You know, we had developed Levittown right after World War II; Levittown is located in Senator D'Amato's town. There was a lot of creative work done by local government during that period to allow some construction standards to change to get a Levittown in. And Levittown is one of the prides, really, of Long Island at this stage. And yet it was creative local government that allowed that project to take place.

Senator CRANSTON. Do you have any other proposals re Federal initiatives that would help?

Mr. McMILLAN. Well, I think some of them that I mentioned, for example, dealing with the infrastructure. Interest rates would be another area in which affordable housing or as we like to call it "entry level" housing would be helped.

Senator CRANSTON. In your testimony you discuss various local decisions, primarily on zoning matters, that contributed to the rapid escalation in housing prices in Long Island. In fashioning Federal legislation to what extent do you feel the Congress should give incentives to local governments to develop more realistic and fairer zoning policies, and what would such incentives look like?

Mr. McMILLAN. Senator, there is an old saying, you can lead a horse to water. You can't necessarily make the horse drink. I think that is the challenge here in dealing with local governments. It is very important that it not be a sledge hammer, but that it be a carrot approach. I think, for example, encouragement of greater density, so there would be greater land use—perhaps some type of incentives in that area. We should consider not only density but creative zoning such as cluster zoning, and zero lot lines.

Remapping towns is a very expensive proposition. For many towns on Long Island, zoning is by exception not by rule. And I think maps could be redone with some Federal Government support as an encouragement for entry level affordable housing. That would be an appropriate approach.

Senator CRANSTON. You mentioned community opposition to various proposals for dealing with housing problems.

What is the nature of that opposition? What are they opposing and what can be done about it, in your opinion?

Mr. McMILLAN. Well, whether it is real or perceived, it is just as real in the eyes of the beholder. There is an attitude situation that relates really to property values. Long Islanders generally feel—bring up the drawbridge, we are in the castle. Not in my backyard—NIBY is an approach on the Island that is used a lot. They left the city and left some problems in the city and don't want those problems brought to the Island. So when you say affordable housing, the immediate reaction is low income housing projects. And that is what creates the problem. Our job at the LIA is education. We are trying to do the best we can to say, we're talking about engineers making $50,000 a year, who cannot afford an entry level house on Long Island. That is the market we are talking, and we need a tremendous amount of education.

Senator D'AMATO. Mr. Chairman, that's exactly the problem that we face. The problem is that in some of the higher-cost areas such as Los Angeles or the New York metropolitan area, where you

With these factors in mind, it became clear that it would take more than just additional funding sources or legislative initiatives to bring about additional affordable housing on Long Island. What must come first is a major educational campaign to change the perception of Long Islanders about the need for affordable housing and its relationship to both the economy and the community. Only by changing perceptions and attitudes can there be any meaningful addition to affordable housing on Long Island.

The housing market on Long Island has reached a point where reasonable alternatives must be developed and implemented to persuade the Long Island community of the importance of this issue, not only to themselves but to all of Long Island. While the LIA has found that some local governments have had some success in attempting to solve the problem, most specifically projects in Manhasset, East Hampton, Southold, Islip and Hempstead, these projects are miniscule in relation to the number of units needed. They do however show that in some communities it is possible for officials of local government to take the initiative to pursue projects of this nature.

Many communities and local governments still do not understand the necessity of pursuing these type of projects with the necessary initiatives and resources. Many of them prefer to wait for judicial determinations on the issue, which have occurred in other areas of the country, including New Jersey, but have not yet reached New York. The LIA does not believe that waiting for judicial decisions, with their long lead time and general lack of direction will lead to meaningful or thoughtful solutions to the problem. Only through the positive actions of governments and the community can this issue be seen as what it actually is, perhaps the dominant issue facing the Long Island economy in the years ahead.

The time is right for a full-fledged move toward a series of initiatives to solve the affordable housing issue on Long Island. The issue of affordable housing has been brought to the forefront through the activities of many individuals and organizations, including the LIA. The time has now come to move from talking about the issue to taking specific actions to increase the amount of affordable housing on Long Island. Without it, our children, our parents, our employees and our employers may find that they cannot and will not be part of the Long Island community any longer.

LIA HOUSING COMMITTEE

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July 1, 1987

PRESENTATION TO SENATE SUBCOMMITTEE ON HOUSING

My name is Cathlene Wells. I teach English at Roosevelt High School in the Los Angeles Unified School District. I am a member of United Teachers-Los Angeles. I am here today to talk with you about the severe difficulties currently involved in a teacher being able to purchase a home for him or herself. I am grateful to UTLA, United Teachers-Los Angeles, for providing the opportunity for me to present these serious concerns to you.

I have been a teacher for 18 years. I taught for 16 years in private Catholic institutions; 13 years of that time I was a Roman Catholic nun, so received no personal financial reimbursement for my teaching. Soon after I left the convent, my father became chronically ill, and I felt I needed to be in a position to earn more money to help with future medical costs. I have now been teaching in the Los Angeles Unified School District for two years.

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Also, most lending agencies prefer 20% down. Some agencies will only lend on a single-family dwelling. I would need to buy something similar to a duplex, since I could not make the $800-900 monthly house payments on my salary alone. I would need to have a renter.

Another problem with duplexes or renting situations is that often the renter is not reliable or does not take good care of the property. This adds an extra stress and burden for the teacher who should, and needs to be able, to spend his or her time planning, evaluating and replanning for the needs of the students. Many of our students are becoming increasingly difficult to reach in a teaching situation because of their very troubled family, economic and personal situations. This requires great creativity and skill on the part of the teacher. Those of us who love teaching love to do this planning and are energized by it, but it is extremely time-consuming. Dealing with an unreliable or unsavory renter would take away precious time that is needed to prepare for the students.

In addition, it is very difficult to find a home between $100,00 and $130,000 in an area of the city where there is a

pride in the way homes are cared for and where a female teacher would feel safe. It is truly impossible for a single female teacher to have any hope of purchasing a home for at least five to ten years after beginning her teaching. This includes living extremely frugally, with very little possibility of money for either relaxation or enrichment, both of which are necessary for all teachers, especially the young who are just beginning.

As I speak, I wonder what person would seriously consider a teaching career now. Could a young man plan to support a family this way? Could a young woman provide for her financial security? Would either one of them want to sacrifice a modest amount of gracious living manifested in their living accommodations, clothing, transportation and recreation while they are saving for a home? Should they be required to? Could a young couple even think of raising a family in this situation?

I have taught for 18 years. I love teaching. I do it well. In all honesty, I must say, I cannot encourage my high school students to join the teaching profession. Most of them do not even consider it because of the difficulties I have described. Our country needs to attract the idealistic, the talented, even the ambitious, to the teaching profession.

I must sadly say, in closing, that I, too, am considering taking my teaching skills and experience to another field which will pay more. I am 40 years old. I need to take care of myself so I will be able to give effectively wherever I am. I desire greatly and think it is prudent to have the financial investment of a home.

I believe we need dedicated teachers for our country's future. I believe education is the key to any society's future. But I do not see how I can teach in our public school system, take care of my money and myself wisely, and take care of my parents as they grow older and ill. I feel we are in a depressing and almost hopeless situation regarding teachers being able to buy their own homes. I think it is an urgent issue to address if we want to attract young, talented teachers to this profession.

I am grateful that this committee is considering this serious need, and I believe it is frighteningly true that we teachers, our country's youth, and our country's solidly-founded future, are dependent upon your deliberations in this matter.

have people who are earning between $35,000 and $50,000, there is no opportunity, as hard as it may seem, to purchase a home. The problem is to galvanize legislation that will attract the support of my colleagues. They say, why should we enter into a program that will, in essence, be subsidizing your high income earners? It is one that I have wrestled with a number of my colleagues and friends on this committee about.

I didn't mean to interrupt, but that is the nub of it. That is really where the issue is. How do you convince people that, really, for young professionals, engineers, coming out of school, starting a family, $32,000, $33,000, are not, today, in a position and will not be in a position to acquire their own home. I didn't mean to interrupt but you hit it, and I thought I should give to you what some of our colleagues share. If you represent a constituency in Idaho or North Dakota or South Dakota, where the median income maybe be $14,000 or $15,000, they have a very real problem in justifying to their constituency a program that would take into account the needs of people who have incomes two and three times that level.

It is a very real dilemma.

Mr. McMILLAN. Absolutely right.

Senator CRANSTON. Thanks Al.

Mr. Brown, there's some people who say that the decline in homeownership affordability doesn't require Federal intervention because the problem will correct itself in time. They generally make four arguments in support of that view, and I would like to ask you to comment on each of them.

First, they say the problem is caused by temporary demographic factors. As the baby boomers age, homeownership rates will rise again.

Do you agree?

Mr. BROWN. Well, I believe that we should, in fact, expect to see higher homeownership rates as the baby boom ages, but that basically masks what, in fact, is the right question to ask. What is happening to the age-specific homeownership rates? As I mentioned earlier and you mentioned in your statement, that the homeownership rates for young households are declining, systematically, throughout the country. That means that a 30-year-old now is less likely to own than the 30-year-old 10 years ago. While the aggregate homeownership rates may go up, the age-specific homeownership rates for young households have been declining, and unless some action is taken, they will continue to decline.

Senator CRANSTON. The second argument is that the Tax Reform Act of 1986 will raise the cost of real rents relative to the cost of homeownership and thus stimulate the purchase of homes.

Do you think that is likely?

Mr. BROWN. I believe the analysis suggests that tax reform will, in fact, make homeownership more attractive than renting in years ahead. But I think the testimony of Ms. Wells really hits to the point of this issue. If I ask her, if we are going to have a 20-percent increase in her rent, is it going to be easier or harder to accumulate the down-payment necessary to buy a home 5 years from now. The answer is clear. With increasing rent it is really quite impossible to expect renters to accumulate the down payment to make the ownership.

I would like to point out that our whole process of creating housing has relied on continued upward mobility of people in the housing market. When we get to a situation where renters are stuck, that is going to, in fact, stop the whole flow of housing for younger households who won't be able to move into the rental housing, and we are going to accumulate a larger and larger problem.

So, I think, the higher rents, rather than making homeownership more attractive, will make it really impossible.

Senator CRANSTON. The third argument is that anticipated growth in real incomes will more than offset the increases in housing prices.

Do you think that is at all likely?

Mr. BROWN. Well, I would love that to be the answer. If I could find forecasts and reliable estimates that income growth would be substantial enough to offset the very serious problem, we might believe that this could be an answer. But, I don't expect it. I don't see any forecasts of household income growing rapidly enough to offset housing costs.

And, furthermore, I think we might expect that if household income rose that fast housing prices would go up as well.

Senator CRANSTON. The fourth assertion made by some is that the invisible hand of the market will eventually solve the affordable housing problems of booming regions. People and economic growth will move somewhere else.

What do you think of that argument?

Mr. BROWN. Well, first of all, I want to point out, that while there are real problems, particular problems in Long Island and Los Angeles and other particular areas, the Boston metropolitan area, those are not the only regions in this country with serious housing price-to-income problems. There are serious problems all over the country. So it is not just a booming region issue.

Second, I think that this ignores the enormous transaction costs that would be required in relocating development and relocating people to other parts of the country.

I submit we must be able to do better than to wait for the invisible hand to solve these kinds of problems.

I am reminded of a paraphrase of John Maynard Keynes. In the long run, it may be OK. But the long run is a long time from now. There is a lot of injury and loss imposed on people.

Senator CRANSTON. Thank you very much

Al, do you have any questions or statements?

Senator D'AMATO. I think John does.

Senator CRANSTON. John, do you have any questions or statements?

Senator CHAFEE. Yes, I have a couple of questions. I don't have a statement, Mr. Chairman.

Mr. McMillan, you mentioned about the possibility of the donation of Federal land. Also, I noticed in your presentation you talked about the attractiveness of Long Island, and you listed on the top of page 3, Long Island businesses are faced every day with refusals from prospective employees, not because of lack of culture, parks, beaches, and golf courses, giving the indication that parks, beaches, and golf courses were an attraction.

Mr. MCMILLAN. Absolutely.

Senator CHAFEE. And I just would caution the enthusiasm for gobbling up Federal lands for housing when every community needs a balance and, as you indicated in your very fine statement, that balance does involve parks and it involves beaches and it involves golf courses.

So first of all, everybody always eyes Federal lands, and that is nice except the Federal Government needs them and that is why they have got them in many instances.

Second, if they are to go, as you know, frequently we in the disposal of them give priority to beaches and parks where everybody has a chance.

So I just hope that the focus always isn't on grabbing them for housing. If you grab the Federal lands for housing, that is a temporary relief, but I am not sure that is a long-term solution.

Mr. McMILLAN. Right. Senator, that is only one of many, but I did indicate that all of that should be done in cooperation with local governments. Local governments, in my opinion, are the key. No matter what subsidy, what incentive, local government has to be a participant.

Senator CHAFEE. Well, I certainly agree with you on that.

Mr. Brown, as you look at the overall situation, the carrying costs namely, the interest rates, are a major factor, I assume, in the lack of affordability for housing. Is that correct?

Mr. BROWN. That is one of the factors, but there are others as well.

Senator CHAFEE. I think it is important to stress that because the high interest rates come from the high deficits. So when the citizens see some in Congress attempt to cut the spending, it isn't just to be Scrooge. One of the most important benefits of that will be reduction in the interest rates.

Do you agree with that?

Mr. BROWN. I think a reduction in the interest rates would help this problem. We did witness some fairly substantial declines in the interest rate over the last 2 or 3 years, and that helped some. But, it really hasn't turned around the situation completely because there are other costs imposed on homeowners, particularly the size of this down-payment and entry costs. These costs are really independent of what the interest rates are. If you can't afford the down-payment, you can't get into homeownership.

Senator CHAFEE. Yes, but the down payment, the points you are talking about are another way for the lender to get something.

Mr. BROWN. Well, there are both real closing costs and real down-payment requirements. These equity requirements have increased over the last few years. Interest rate reduction alone won't solve that problem.

It helps, Senator, I agree. The real issue here is the size of the real interest rate, which reflects concern about inflation and the hedging of that inflation by keeping a higher real interest rate. Anything that we would do, including reducing the size of the deficit, to make people more confident about our ability to keep inflation down would lower the real interest rate lower and would help homeownership.

Senator CHAFEE. In your comments you seem to indicate that the cost of construction has not been a major factor in the increase. In other words, while it has gone up, it hasn't gone up that much.

If you look at the price of a house now, the price of an average house in the United States is something like $110,000. Starting with just the raw piece of land and then building, what is the major factor in the increases—the price of land?

Mr. BROWN. The price of land has been the most significant.

Senator CHAFEE. And the carrying costs, the financing?

Mr. BROWN. The interest, the financing on the construction period. Those two have been the largest components of the increase in cost. Land is the most significant of those.

Senator CHAFEE. I don't see any solution to the land problem. Take Mr. McMillan's situation in Long Island, if you have more and more people crowding into a finite area, the law of supply and demand is going to make the price of land go up, isn't it?

Mr. BROWN. I think so, although I think that he had some suggestions. I would echo those and encourage us to look at the experiments that were done about building more affordable housing. Those experiments suggested that there were changes in the process of building by local governments that could have up to 20, 30 percent drop in the cost of building houses.

Those will directly translate to the cost of land. At the present time what we have done is to make land harder to build on and therefore a more expensive part of building housing.

I think we should look for ways of providing the right incentives, finding out why it is local governments actually are not adopting those kinds of changes that could affect the cost of building.

We can find ways, I think, to lower the cost, and all of that will direct offset land prices.

What I am saying, Senator, is that while I believe supply and demand is fundamental, the escalation in land price is not correlated perfectly with the growth in population and limited supply of land. It is more correlated with local regulations that don't provide that land for development in the way it could.

Senator CHAFEE. Well, I think the ideal situation would be that every community, no matter whether it is three-acre zoning or whatever, would be required to have a certain portion of high density low income housing, which would thus increase the supply of available housing, and then there are all kinds of fringe benefits, I think, with the mixture of the low income children into the school system there rather than the concentration of all the low income people in one area.

But then you get into land planning or community planning, which is an absolute no-no up here, and maybe Mr. McMillan is right, that somehow there has to be a carrot out there to get the communities to do that.

Thank you.

Mr. BROWN. I might say one other thing. It is not just the low income housing. Local regulations affect the size of the streets, the curbs, the sidewalks. Changing those requirements can change the cost of providing housing.

Senator CHAFEE. Thank you.

Thank you, Mr. Chairman.

Senator CRANSTON. Thank you.

Al.

Senator D'AMATO. Mr. Chairman, first of all, let me commend you for addressing this important issue, the question of affordable housing for our working families, for our young professionals today.

I am afraid to say to you, Mr. Chairman, but I have seen it and it has been demonstrated to me, that our colleagues really do not have an appreciation for this. They are out of step with reality as it relates to the purchasing of homes and what it takes, whether it be in Long Island or whether it be in other parts of our country, and it is just not taking place, and the reason those figures are coming down is because given the growth and the cost factors as it relates to the price of a home and given the increase in revenues, they just have not kept pace.

In our own area, as Mr. McMillan, who has done—and let me commend Mr. McMillan for his efforts in attempting to focus on these problems, and he has done it well, and for searching for some possible solutions, and I do believe that the local government does have the most significant area of contribution to make in attempting to make entry level housing possible.

They do have and should continue to have that responsibility, but we have ways in which we can help, and I am not suggesting making available Federal lands. I think—and I agree with Senator Chafee—that that would be almost an impossible task, given the constraints that are placed in the law, with public use being first, Federal use and other public uses, et cetera. It is not the answer.

However, it would seem to me that in our tax code, we have set back—and I am not suggesting to you that there were not many necessary reforms, but we have placed a major impediment as it relates to the construction of rental housing, which then obviously affects the individual home construction industry.

And let me ask you, Mr. Brown, have you analyzed the tax code as it relates to housing, rental housing, and if you have, what opinions have you come up with? Has it made it and will it make it more difficult to construct rental housing?

Mr. BROWN. We believe it will make it more difficult to construct multifamily housing. We don't believe we have seen the full impact of tax reform. What we have seen under construction so far in 1987 was put in the pipeline in 1985 and 1986.

We expect that the tax reform will in fact have a very negative effect on rental.

Senator D'AMATO. Let me ask you, have you observed whether or not there have been any impact as it relates to the tax code and some of the restrictions that were placed as it relates to first-time home buyers?

For example, in New York we have what we call the Sony Mae program, which writes down the interest, gives us low interest, and what we are finding, what we are experiencing—and I don't know if you have made an analysis in other areas—that many of the first-time home buyers, their income is too high, yet the cost of the home is beyond that without that Sony Mae and they are disqualified.

Mr. **Brown**. Yes, I think that we simply have gaps in these kinds of programs that make it difficult for people in these middle ranges to get access to them. The alternative is that they can't really get into homeownership.

Senator D'**Amato**. And while their income—while others who are below that income simply do not have enough to be able to sustain the purchase of a home?

Mr. **Brown**. Yes, I agree.

Senator D'**Amato**. There is that gap.

Mr. **Brown**. Yes, I agree. But I want to also emphasize that, if the down-payments are larger, even with low interest rates I can't get into the purchasing.

We can examine ways of encouraging young people to save more, which is in our national interest and will help the interest rate, in the hopes of accumulating that down-payment. Those programs I think have some value.

Senator D'**Amato**. Mr. Chairman, I have just received a message. We are in that banking conference, and they have asked me to get over there, but let me again congratulate you.

Let me thank Mr. McMillan for his work because certainly Long Island is not unique as it relates to the problem, the affordability of housing for young people, young professionals, our engineers who work at some of our industrial complexes, that these complexes can no longer attract them. They feel that the housing costs have become so significant and so high that it becomes beyond their ability.

As a result, we are experiencing business relocating to other areas, and so I think there does come a very real responsibility that local government has got to participate, but we have got to help close those gaps, for example, in the mortgage programs that do exist to make them more workable.

Senator **Cranston**. Thank you very much, Al.

We thank the three of you very, very much for your helpful participation. I'd like to say to you, Mr. McMillan, that both Al D'Amato and John Chafee raised concerns about your proposal about public Federal lands. And it seems to me that idea might have merit and should be explored. I share their views about preserving that for public purposes—beaches and parks, and so forth.

But this is apublic purpose, to promote housing. If that's the way to get affordable land so we can get affordable housing, I should think we should explore it.

There are obviously many military bases close to heavily populated centers. And it's hard to get land from them. But, maybe, upon occasion, that could be accomplished.

Thank you all very much.

Mr. **McMillan**. Thank you.

Senator **Cranston**. Thank you.

Mr. **Brown**. Thank you.

Senator **Cranston**. Will the members of panel two please now come forward.

Senator **Chafee**. Mr. Chairman, in this gap while the other panel is coming, I would like to extend my thanks also to you for holding these hearings. I think it is splendid that you are doing this, and we may not solve all the problems here but we will certainly get a better handle on it hopefully, and I want to congratulate you.

Senator CRANSTON. Thank you very much. I appreciate that.

We have embarked upon a very carefully laid out course of action designed to lead us to some significant legislation. It is going to take a lot of hard work and time, but I am very hopeful we can come up with some very significant legislation with the help of a lot of people by early next year.

Our first witness from this panel is Ardath Cade, Assistant Secretary for Housing and Community Development for the State of Maryland, Annapolis, MD.

I want to say that Senator Sarbanes sends his regrets that he will not be able to attend this morning's hearing because he must chair a hearing before the Joint Economic Committee. He extends his thanks to the witnesses for their testimony and particularly want to welcome Ardath Cade from the Maryland Department of Housing and Community Development. Senator Sarbanes informs me that Mrs. Cade has been Assistant Secretary of Housing and Community Development since 1979 and has a distinguished career in State and local government in Maryland. She has played a major role in developing and implementing innovative new programs to address the housing needs of the State's low and moderate income citizens. The variety of State housing programs in Maryland is impressive and a tribute to Mrs. Cade and other State leaders who have developed creative solutions to housing problems. The State has actively used mortgage revenue bonds and other State and Federal resources to provide low interest loans and other services to encourage homeownership. In addition, Mrs. Cade coordinated the successful effort last yeat to enact new programs to assist groups such as the homeless and handicapped with special housing needs.

STATEMENT OF ARDATH CADE, ASSISTANT SECRETARY FOR HOUSING AND COMMUNITY DEVELOPMENT, ANNAPOLIS, MD

Mrs. CADE. Thank you very much, Mr. Chairman, for this opportunity to be here, and we always thank Senator Sarbanes for his interest as well as this committee's interest in our concerns about housing.

I am Ardath Cade, of the Maryland Department of, Housing and Community Development, which just today has become a cabinet level department of Maryland State government. This is an action one of the first legislative initiatives of our new Governor, William Donald Schaefer, who has long shown an acute interest in housing.

Maryland can be seen as America in miniature, a State of contrasts.

For instance, Montgomery County, just adjacent to D.C. is one of the Nation's wealthiest, where despite very innovative efforts by the local government many people cannot afford housing.

Urban Baltimore is a national model for creative neighborhood and housing revitalization, using every Federal and State dollar available, and creating public and private partnerships, but still they have a high rate of homelessness and too low a level of homeownership.

Our rural areas, such as Garrett County in the Appalachian Mountains and many of our Eastern Shore counties, are desperately lacking in code standard housing.

I feel that in each of your States you experience these same contrasts, but let the first point be made, that all areas, rich, poor, urban, and rural, have persistent housing problems that demand the attention of government at all levels.

Second, despite the focus in today's hearing on homeownership, let us acknowledge that housing issues cannot be segmented into neat homeownership and renter policies. Housing is a continuum, and actions which affect rental housing generally affect homeownership patterns as well.

For example, seemingly unrelated actions, such as limiting the historic preservation tax credit for income producing property, has decreased the supply of rental housing, as have several of the other real estate provisions of the Tax Reform Act.

The decrease in supply drives up rent levels, thereby consuming a greater percentage of income and decreasing a young family's ability to accumulate the down payment for a home.

Likewise, the ceiling on issuance of tax-exempt bonds has seriously curtailed the State's ability to provide homeownership opportunities to its low income citizens and may limit the usefulness of the State's own financial assistance tools that work in concert with tax-exempt bonds.

Third, there is a critical need for a long-term reliable Federal housing policy, and we are especially grateful to you for your interest in hearing our concerns as you take steps to formulate such a policy.

Fourth, in the specific area of homeownership the key problem for most renters seeking to buy is affordability. Homeownership is still out of the reach for a majority of Marylanders. About 45 percent of the families in Baltimore city cannot afford to buy a $40,000 home, and in certain rural areas over 70 percent of the residents can't afford the median priced home.

We are here to urge you to take steps at the Federal level to expand opportunities for homeownership for low and moderate income families, but not without the State being a partnership in creating that opportunity. I think as you continue to look you will see that many, many States have expanded their initiatives as partners with the Federal Government and local government in taking responsibility for housing in recent years.

In Maryland we have two major State-funded programs to promote and maintain homeownership. Our department includes not only our Housing Finance Agency and community assistance groups, but also a mortgage insurance program, not unlike FHA, called the Maryland Housing Fund. It is this program that has been especially helpful in our being able to offer homeownership opportunities that exceed the limitations of FHA and private mortgage insurers.

The Maryland Housing Fund initially started in response to the unwillingness or inability of FHA and the PMI's to meet the financing needs of inner cities. The fund was created by issuance of general obligation bonds, the proceeds of which were placed in dedicated reserves, with insurance ratios established relatively similar to industry standards. Those reserves now total over $70 million.

Although this insurance program has not been rated separately as an insurance program, it has consistently met the scrutiny of Moody's rating agency as a sound security for the issuance of tax-exempt revenue bonds both by our State Housing Finance Agency and by the Montgomery County Housing Opportunities Community.

The Housing Fund can provide both primary and pool insurance. Its rates can be somewhat lower than PMI's because it does not have to yield a profit and its reserves are generated from State appropriations rather than from traditional capital sources.

An important difference between FHA and the Maryland Housing Fund is that 95 percent of our loans are high risk loans, while 30 percent of FHA's are high risk, or over 95 percent loan-to-value ratio.

Further, the Housing Fund has, through its high risk pool, insured special targeted programs, wherein the purchase price and rehab costs are added together for well over a 100-percent loan-to-value ratio.

We are in no way suggesting the Maryland Housing Fund or any State mortgage insurance program as being a substitute for FHA, but instead a useful supplement.

We also have a State-funded mortgage program which can make mortgages as low as 4 percent to households with incomes up to $18,000. We are trying to tie these loans and funds to local government and nonprofit efforts to respond to particular low housing needs. During 1986, the average household income of recipients was $14,800.

What are we asking of the Federal Government?

First, there are things we must keep. It is critical that the sunset provision on mortgage revenue bonds be repealed. This program has helped over 16,000 Maryland families buy homes. The average income of those families last year was $24,000.

Also, the volume cap on tax-exempt revenue bonds has been devastating in Maryland. In 1985, our housing issuance was $1.1 billion. In 1987, it is limited to $167 million, only 15 percent of the earlier total.

FHA, second, must be kept a viable, active insurance vehicle.

Third, we need to continue to be able to use UDAG for creative housing programs, which has been especially true in the city of Baltimore.

Fourth, Neighborhood Reinvestment, which stimulates concrete operational programs such as Neighborhood Housing Services, should be funded at a level to continue the stimulus of private sector neighborhood partnerships.

In addition, we suggest there may be an additional Federal stimulus to homeownership through such approaches as allowing IRA funds to be usable for housing entry fees—closing costs and down payments—or, if this approach is not workable, to have the Federal Government provide some sort of a settlement expense loan program that could be insured by a pilot FHA program; or some sort of a declining value voucher that could be applied to home purchase.

Also, we suggest that there may be a case for housing incentive funds to States, to be used for their particular housing needs in conjunction with their local governments, with the State governments making a contribution.

I thank you for this opportunity to present some of our concerns and our sense of the need for partnerships between the Federal Government and State governments in resolving some of our acute homeownership problems.

Senator **CRANSTON**. Thank you very much.

Mrs. **CADE**. Thank you.

[The complete prepared statement of Ardath M. Cade follows:]

MARYLAND DEPARTMENT OF HOUSING AND COMMUNITY DEVELOPMENT

ARDATH M. CADE'S TESTIMONY

before the

Senate Subcommittee on Housing and Urban Affairs

on

Wednesday, July 1, 1987
at 9:30 a.m.

Dirksen Senate Office Building
Room 538

I am Ardath Cade of the Maryland Department of Housing and Community Development - which just today has become a cabinet level department of Maryland State government. Our new Governor, William Donald Schaefer, recognized that the housing issues in our State are as compelling as human resources, health, environmental and economic issues and, therefore, as one of his first legislative initiatives successfully proposed the creation of this department, which heretofore had been linked with economic development.

Maryland can be seen as "America in Miniature." Close by is Montgomery County, one of the nations wealthiest where, despite the conscientious efforts of the local government, affordable housing is all too often out of the reach of many of the service workers and other job holders in that jurisdiction.

Urban Baltimore, a national model for creative neighborhood and housing revitalization, utilizing every available federal and state dollar, while creating ingenious partnerships with private developers, nonetheless continues to face long waiting lists for Section 8 rental units, a concentration of the state's homeless and too low a level of homeownership, compounded by a tax rate about twice that of any other Maryland community.

Rural areas such as Garrett County in the Appalachian Mountains continue to face a lack of code-standard housing for its low income population, while another rural area, Talbot County on the Eastern Shore has been "discovered" for its gracious water oriented living and is facing tremendous cost escalation without a commensurate increase in income of the vast majority of low income households. Just across the border in the southern end of Prince George's County and in Charles County, far too many households, many of them owner occupied, are without indoor plumbing because of soil conditions that make traditional septic systems unworkable, while the more elaborate disposal systems have been too costly.

I feel certain that in each of your states you experience these same contrasts, but let the first point be made - that all areas - rich, poor, urban and rural - have persistent housing problems that demand the attention of government at all levels.

Secondly, despite the focus in today's hearings on homeownership let us acknowledge that housing issues cannot be segmented into neat homeownership and renter policy areas; housing is a continuum and actions which affect rental housing generally affect homeownership patterns as well. For example, limiting the historic preservation tax credit for income producing properties - including rental housing - has decreased the supply of rental housing, as have several of the other real estate provisions of the tax reform act. The decrease in supply drives up rent levels, thereby consuming a greater percentage of income and decreasing a young family's ability to accumulate the downpayment for a home. Likewise, the ceiling on issuance of tax exempt bonds has seriously curtailed a state's ability to provide homeownership opportunities to its lower income citizens - and may limit the

usefulness of the state's own financial assistance tools that work in concert with tax exempt bonds.

Thirdly, there is a critical need for a long term reliable federal housing policy - and we are especially grateful to you for your interest in hearing our concerns as you take steps to formulate such a policy. There have been some policy makers who have appeared to believe that cutting housing programs can retire the National debt. We feel instead that it will in fact exacerbate the debt.

-- Housing creates jobs; jobs create taxes. For example, in FY 86 the 33,000 single family homes constructed in Maryland created $1 billion in direct wages.

-- Each house built in Maryland last year created approximately $4,500 in new direct sales, income, transfer and property taxes for our State.

-- Strong homeownership patterns create more stable communities with lower crime rate.

Finally, in the specific realm of homeownership the key problem for most renters seeking to buy a home is affordability.

Family incomes have lagged far behind housing prices - e.g. the average sale price of a home last year increased 10% while incomes rose only 6.3%. (Federal Bureau of Labor Statistics)

Despite interest rates well below those of a few years ago, homeownership is still out of the reach for a majority of Marylanders. About 45% of the families in Baltimore City cannot afford to buy a $40,000 house. (The Baltimore Regional Planning Council, 1985) In D.C. suburban Montgomery County in 1984

Senator CRANSTON. We will now hear from Terry Duvernay, executive director of the Michigan State Housing Development Authority.

We welcome you, Mr. Duvernay.

STATEMENT OF TERRENCE R. DUVERNAY, EXECUTIVE DIRECTOR, MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY, LANSING, MI

Mr. DUVERNAY. Thank you, Mr. Chairman and members of the Senate Subcommittee on Housing and Urban Affairs.

I would like to thank you again for the opportunity to testify before you today.

I am Terry Duvernay, executive director of the Michigan State Housing Development Authority, MSHDA, a housing finance agency established by the Michigan Legislature a little more than 20 years ago to address the housing needs of our State's low and moderate income families and senior citizens.

Affordable homeownership is becoming a contradiction in terms, an oxymoron, if you will, for families with modest incomes.

If you are a low income wage earner, you cannot compete for a mortgage in the conventional market today.

If your down payment is less than 10 percent, you will not be able to obtain private mortgage insurance for your loan.

If FHA insurance or a VA guaranteed loan or a low interest Housing Finance Agency loan is not available in your community, you have few options.

Rising interest rates and higher home prices are putting homeownership farther and farther out of the reach of moderate income families.

In Michigan, home prices rose an average of 9.16 percent in 1987, compared with the first 5 months of 1986, and home sales dropped 9.9 percent.

The demand for the available supply of reasonably priced homes will increase as the baby boomers come of home buying age. In 1980, about 3 million Michiganites were in their midtwenties to midforties. That number rose to 3.2 million last year and is projected to 3.3 million in 1991.

Despite their media reputation as affluent yuppies, large numbers have incomes below the median. Forty-two percent of the 25- to 34-year-old households earned less than $25,000 in 1987, a fifth of them less than $15,000.

Single parent families with modest incomes and child care expenses are among the most severely affected.

Tighter underwriting criteria and higher down payment requirements add to the obstacles faced by first-time home buyers. The refusal of private mortgage insurance companies to approve loans with less than 10 percent down payments has significantly hampered MSHDA's lending program.

One company refuses to write insurance on our loans in the four most populous Michigan counties if the down payment is only 5 percent.

The 1986 Federal Tax Reform Act is still another blow, by adding volume caps, an alternative minimum tax, and bond registration requirements that will make it harder to raise capital for mortgage financing, and looming ahead is the 1988 sunset for mortgage revenue bonds.

The Authority has taken a number of steps to increase homeownership opportunities: financing of existing homes; recycling loan prepayments into a $5 million fund to offer 6.5 and 7.5 percent interest loans to very low income families; establishing the Nation's first full service statewide mortgage credit certificate program, the Michigan Mortgage; funding a $1 million competitive grant program that assists neighborhood organizations with grass-roots housing activities, including renovation and resale of homes to low income families; providing interest free loans for larger neighborhood revitalization projects in several cities; and setting aside up to $9 million in end loans to help buyers in neighborhood resale programs.

In its direct lending and mortgage credit certificate programs, MSHDA has helped more than 23,000 families with average incomes well below the State median buy reasonably priced new and existing houses in almost every county and in many of our distressed cities.

As innovative as MSHDA is and as skilled as we have become in leveraging our dollars, however, we still need Federal tools to help us.

We strongly urge extension of mortgage revenue bonds to 1992, continued adequate funding of FHA and VA loan programs under Government and not private direction, establishment of a Nehemiah Housing Opportunity Grant Program, and Federal support for urban homesteading and community development block grants.

Many of us who are homeowners may have been assisted by Federal loan programs. All of us benefit from the Federal tax deductions specifically placed in the Tax Code to encourage homeownership. We cannot in good conscience now slam the door on first-time home buyers by ending revenue bonds, curtailing Federal insurance programs, and underfunding community based programs that assist them.

I cannot stress too strongly that the Federal Government cannot turn over housing responsibility to the States and at the same time continue to remove the tools we must have to carry out those responsibilities.

I appreciate your efforts, Mr. Chairman, along with Senator Riegle, in looking at new ways to encourage homeownership. Allowing first-time home buyers to use their IRA funds to purchase homes, for instance, is innovative and represents the new type of thinking that is needed.

Thank you very much.

[The complete prepared statement of Terrence R. Duvernay follows:]

one-half of the families cannot afford a 9.5% mortgage on the area's average priced home - then well over $110,000 - and now over $122,000.

Average cost in rural Talbot County has escalated to nearly $100,000, far out of the reach of 70% of the families.

We are here to urge you to take steps at the federal level to expand opportunities for homeownership for our low and moderate income families, but not without the state being a partner in creating that opportunity.

In Maryland, we have two major state-funded programs to promote and maintain homeownership.

Before elaborating on those programs let me briefly describe our housing department.

Unlike most states we include both the Housing Finance Agency and the community development programs within a line agency. The director of our housing finance programs, instead of reporting to an independent board, reports to the Department Secretary, just as does the director of the office that includes CDBG, CSBG, housing technical assistance and many other typical community affairs programs. This allows for the greatest efficiency and coordination in linking state funds and revenue bond financing, and allows for a unified housing policy emanating from a single state agency rather than the dichotomy that occurs in some states. (We feel fortunate that in the early 70's when the finance agency was formed, Maryland was going through a process of consolidation of several hundred independent commissions into less than 15 cabinet level departments and thus the housing finance agency too

was included in a line agency).

Along with Housing Finance and Community Assistance, our department also includes a mortgage insurance program, not unlike FHA. It is this program that has been especially helpful in our being able to offer homeownership opportunities that exceed the limitations of FHA and private mortgage insurers.

The Maryland Housing Fund initially started in the early 70's in response to the unwillingness or inability of FHA and the PMI's to meet the financing needs of inner-city areas.

The Fund was created by issuance of General Obligation Bonds, the proceeds of which were placed in dedicated reserves, with insurance ratios established relatively similar to industry standards - e.g. the ratio in the main homeownership fund is 1 to 25, whereas in the high-risk "Pilot Program" homeownership reserve the ratio of reserve to insurance in force is 1 to 15. Yet another reserve stands behind insurance on multi-family rental projects and fourth and fifth reserves are used for multi-family and single family rehabilitation projects. Over the years, the state has appropriated about $49 million to the reserves, through general obligation bond authorizations and general fund appropriations. Furthermore, the interest earned on the reserves is added to the reserves, which now total over $70 million.

Defaults have been paid off throughout the history of the Housing Fund from operating funds - i.e. premium payments; the reserve funds have never been called upon.

Although this insurance program has not been rated separately as an insurance program, it has consistently met the scrutiny of

Moody's rating agency as a sound security for the issuance of revenue bonds, both by our State housing finance agency (the Community Development Administration) and by the Montgomery County Housing Opportunities Commission.

How has the existence of this State mortgage insurance program aided our efforts to encourage homeownership?

The Housing Fund can provide both primary and pool insurance. Its rates can be somewhat lower than PMIs because it does not have to yield "profit" in the same way as PMI, and its reserves are generated from state appropriations rather than from traditional capital sources. (Rates for primary insurance are three quarters of one percent for the first year and one quarter of one percent annual renewal premium thereafter on the original loan amount. Rates for pool insurance have varied from 2 to 12 1/2 basis points.)

An important difference between FHA and the Maryland Housing Fund is that 95 percent of our loans are high risk loans while 30 percent of FHA's are high risk.

The Housing Fund in many instances assumes risk of loss at nearly 100% of the mortgage, thereby minimizing the need for large downpayment.

Further, the Housing has, through its high risk pool, insured specially targeted programs - e.g. purchase price plus rehab costs for over 100% loan to value ratio.

Although the Fund has, of course, experienced claims, the rate of claims historically has not been as high as FHA's despite the apparently greater risk. This may be due in part to the fact

that these targeted programs are often generated through neighborhood non-profit organizations which provide housing counselling before and after the home purchase.

Overall, the Maryland Housing Fund is more pro-active than FHA; it is able to tailor its response to specific needs, rather than rely on universally applied programs.

We are in no way suggesting the Maryland Housing Fund - or any state's mortgage insurance program - as being a substitute for FHA, but instead a useful supplement.

A second state-financed homeownership program is the Maryland Home Financing Program. Like the Housing Fund, it has been funded over the years through GO Bond funds and general appropriations, neither of which must be paid off by the mortgage repayments. Instead, the mortgage repayments constitute a revolving fund which now yields over $10 million annually for new mortgages. In this program, since the mortgage rate need not be tied to bond interest rate as with revenue bond programs, we are authorized to make mortgages to as low as 4% based on the income of the household, which are capped at $18,000. We are trying to tie these loan funds to local government and local non-profit efforts to respond to particular community housing needs. During 1986, the average houehold income of recipients of these loans was $14,800.

Maryland is not alone in "investing" state funds into homeownership programs. Massachusetts, through the Massachusetts Housing Partnership, offers the Homeownership Opportunity Program (HOP), tying community inducements for affordable housing (e.g. low cost land or zoning incentives) with revenue bond financing bought down to as low as 5% by Partnership funds, with developers agreeing to sell about half the units at affordable prices, which may be as much as 30 - 50% below median.

A New Jersey Lease Purchase Program helps low to moderate income people build up a downpayment while living in the home, by applying part of their rent to this purpose for a three-year period.

What are we asking of the federal government?

First, there are things we must keep --

1. It is critical that the sunset provision on mortgage revenue bonds be repealed. Without federal action this program will terminate in 18 months. This program has been critical in Maryland in helping families who generally earn $18 - 25,000 buy homes. Last Monday we made over $40 million available through over 20 lenders statewide. Within three days only $3 to 5 million (mostly allocated to the rural areas) had not been pre-committed. Without Mortgage Revenue Bonds, over 16,000 families in Maryland would not have been able to afford a home of their own. Last year's average family income in this program was $24,000. Additionally, the volume cap on tax exempt revenue bonds should be reconsidered. Maryland housing bond issuance in 1985 was $1.1 billion; 1987's authorization is $167 million, only 15 percent of 1985's total. This federal tax policy clearly has been devastating to our efforts to provide affordable housing.

2. FHA must be kept a viable active insurance vehicle. We would also encourage that standards be reviewed as they relate to lower income households. Reportedly, also, their diligent

enforcement of highly defined property standards serves to discourage sellers willingness to "sell FHA."

3. We need to continue to be able to use UDAG for creative housing programs. In Baltimore, the city has provided UDAG-funded soft second mortgages, behind our state CDA first mortgage to establish homeownership opportunities for some very low income persons, and owner-occupied housing in neighborhoods where this is greatly needed (generally if the owner retains ownership for more than 10 years the second mortgage is forgiven).

4. Neighborhood Reinvestment which stimulates concrete operational programs such as Neighborhood Housing Services and Mutual Housing should be funded at levels to allow its continued stimulus of private sector and neighborhoods in partnership solutions of housing problems.

In addition to things we must keep, we suggest that there be additional Federal stimulus to homeownership through such approaches as:

1. Allowing IRA funds or a parallel tax deductible deposit to be useable for "housing entry fees" i.e. down payments and closing costs. These costs are the most onerous barrier to entering homeownership, e.g. in Annapolis, Maryland, assuming a 10% downpayment and typical Maryland closing costs which include prepayment of a year's taxes plus recordation tax, transfer tax and other conventional fees, the costs at closing on a $100,000 house total about $17,200.

2. If the IRA approach is not workable it has been suggested that the federal government provide funds for a settlement expense

loan program, insured by a pilot FHA program. (The second lien in many conventional situations would disqualify the approval of the first mortgage). Such a program could be aimed at persons at 50-80% of median with stable employment histories, but who cannot meet normal downpayments or underwriting ratios.

3. Yet another approach is a declining-value voucher that can be applied to home purchase instead of rent.

Also, we suggest the potential effectiveness of "housing incentive funds" - an allocation to state governments to be matched by state effort and tied as well to local government initiative, for uses appropriate to the user state in responding to their particular low income housing needs - in both rental and homeownership situations. Maryland for instance might well want to respond to the burden of our high closing costs while another state with state low interest mortgage funds might wish to use the funds to buy down mortgage rates.

Homeownership is declining in a nation that strongly affirms the value of homeownership. We realize that there are no easy solutions to the inability of our lower income households to achieve homeownership. We believe, however, that in this wealthy nation, we must establish and maintain federal policy that contributes to achieving that national value.

Thank you.

TESTIMONY OF THE
MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY
BEFORE THE
SENATE SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS

DELIVERED BY

TERRENCE R. DUVERNAY

EXECUTIVE DIRECTOR
MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY

July 1, 1987

Mr Chairman, Members of the Senate Subcommittee on Housing and Urban Affairs: Thank you for the opportunity to testify before you today.

I am Terrence R. Duvernay, executive director of the Michigan State Housing Development Authority (MSHDA), a housing finance agency established by the Michigan Legislature in 1966 to address the housing needs of our state's low and moderate income families and senior citizens.

Affordable homeownership is becoming a contradiction in terms for families with modest incomes.

If you are a low-income wage earner, you cannot compete for a mortgage in the conventional market today.

If your down payment is less than 10 percent, you will not be able to obtain private mortgage insurance for your loan.

If FHA insurance or a VA guaranteed loan or a low-interest HFA mortgage is not available in your community, you have few options.

Rising interest rates and higher home prices are putting homeownership farther and farther out of the reach of moderate income families.

In Michigan, home prices rose an average of 9.16 percent in 1987, compared with the first five months of 1986--and home sales dropped 9.9 percent.

The demand for the available supply of reasonably priced homes will increase as the Baby Boomers come of homebuying age. In 1980, about 3 million Michiganians were in their mid-twenties to mid-forties. That number rose to 3.2 million last year and is projected to 3.3 million in 1991.

Despite their media reputation as affluent Yuppies, large numbers have incomes below the median. Forty-two percent of the 25 to 34-year-old households earned less than $25,000 in 1987; a fifth of them less than $15,000.

Single parent families with modest incomes and child care expenses are among the most severely affected.

Tighter underwriting criteria and higher down payment requirements add to the obstacles faced by first-time homebuyers. The refusal of private mortgage insurance companies to approve loans with less than 10 percent down payments has significantly hampered MSHDA's lending program. One company refuses to write insurance on our loans in the four most populous Michigan counties if the down payment is only 5 percent.

The 1986 Federal Tax Reform Act is still another blow, by adding volume caps, an alternative minimum tax, and bond registration requirements that will make it harder to raise capital for mortgage financing. And looming ahead is the 1988 sunset for mortgage revenue bonds.

The Authority has taken a number of steps to increase homeownership opportunities: financing of existing homes; recycling loan prepayments into a $5 million fund to offer 6.5 and 7.5 percent interest loans to very low income families; establishing the nation's first full-service, statewide mortgage credit certificate program, the Michigan Mortgage; funding a $1 million competitive grant program that assists neighborhood organizations with grass-roots housing

Senator CRANSTON. Thank you very much. I appreciate your testimony a great deal.

We will now hear from Orest T. Dubno, executive director of the Connecticut Housing Finance Authority.

Mr. Dubno.

STATEMENT OF OREST T. DUBNO, EXECUTIVE DIRECTOR, CONNECTICUT HOUSING FINANCE AUTHORITY, ROCKY HILL, CT

Mr. DUBNO. Thank you, Mr. Chairman, for holding these hearings and giving us an opportunity to testify.

Housing is Connecticut's No. 1 problem. We live in a State with the highest per capita income in the Nation. We are enjoying the lowest unemployment rate in the Nation, and our economy overall is extremely healthy.

But housing is a problem. We in Connecticut are responding to that problem.

The Governor in his budget has provided for funds for not-for-profit developers in order to stimulate the production of housing.

The Connecticut Legislature has formed a special committee, Select Committee on Housing, and they are changing some of the Connecticut laws in order to stimulate production of housing.

Connecticut business and industry is also responding. Some of the largest banks in Connecticut have pooled approximately $100 million together to provide an equity fund in order to try to stimulate the use of the low income housing tax credit.

We in the Connecticut Housing Finance Authority and the Department of Housing have literally gone on the road trying to stimulate the production of rental housing.

I must echo Mrs. Cade's comments about the fact that all housing issues are interrelated, and if we are to speak of a housing crisis, it is very nice to focus on the first-time home buyers, but the production of rental housing, the cost of housing, the cost of financing have to be addressed at the same time.

In Connecticut, since the 1986 Tax Reform Act, we have continued to try to play an active role in assisting the first-time home buyers. Since January 1985, we have provided $478 million in loans to some 6,000 Connecticut families. Of those 6,000 loans, 5,700 of them were to first-time home buyers, 95 percent of them, and while my written testimony has all sorts of statistics I would just like to give you a few.

The average purchase price in the Connecticut market that we finance was $70,000. The down payment was approximately $8,000, providing for a loan of $62,000.

The interesting thing is that the average household income of those 5,700 loans was $27,000 in a State that has a median income approaching $40,000. In the city of Stamford, the median income is $54,000. So whatever few loans that we did make in Stamford it was to individuals of 50 percent of median.

The prospects for homeownership for households that have traditionally been in the market for their first-time purchases has become more difficult in recent years in Connecticut. The excess demand for starter homes on the tax lots greatly exceeds the supply, pushing the prices for these homes to a level that only the most affluent of these households can afford.

Condominium ownership provides an affordable alternative to many; however, the prices of many of these units are beginning to escalate beyond the reach of many first-time buyers.

The most affordable homeownership alternative for many first-time purchasers is in multifamily structures that were previously rental housing. This places the demands of first-time buyers in direct conflict with the need to maintain an adequate supply of affordable rental housing for these renters that are trying to save for their first-time purchase or those who may never choose to be able to afford ownership.

I would therefore make three basic suggestions to the committee.

First of all, support the passage of legislation extending the sunset date for the mortgage revenue bonds for another 4 years or perhaps eliminate it altogether.

Free both multifamily and single family housing bonds from the current overall limitations on State and local private activity debt and place them in a separate housing cap.

Perhaps support and develop some workable and effective equity incentives to encourage the development of affordable rental housing, even if it is not strictly for low income persons.

Make sure that FHA is there to provide the invaluable services they do, and perhaps, as Senator Dodd has suggested in the past and the other two speakers have alluded to it, allow IRA accounts to be used as down payments for housing.

Again, Mr. Chairman, I thank you for the opportunity to testify.

[The complete prepared statement of Orest T. Dubno follows:]

ACTIVITIES, INCLUDING RENOVATION AND RESALE OF HOMES TO LOW INCOME FAMILIES; PROVIDING INTEREST-FREE LOANS FOR LARGER NEIGHBORHOOD REVITALIZATION PROJECTS IN SEVERAL CITIES, AND SETTING ASIDE UP TO $9 MILLION IN END LOANS TO HELP BUYERS IN NEIGHBORHOOD RESALE PROGRAMS.

IN ITS DIRECT LENDING AND MORTGAGE CREDIT CERTIFICATE PROGRAMS, MSHDA HAS HELPED MORE THAN 23,000 FAMILIES WITH AVERAGE INCOMES WELL BELOW THE STATE MEDIAN BUY REASONABLY PRICED NEW AND EXISTING HOUSES IN ALMOST EVERY COUNTY AND IN MANY DISTRESSED CITIES.

AS INNOVATIVE AS MSHDA IS AND AS SKILLED AS WE HAVE BECOME IN LEVERAGING OUR DOLLARS, HOWEVER, WE NEED FEDERAL TOOLS TO HELP US.

WE STRONGLY URGE EXTENSION OF MORTGAGE REVENUE BONDS TO 1992, CONTINUED ADEQUATE FUNDING OF FHA AND VA LOAN PROGRAMS UNDER GOVERNMENT AND NOT PRIVATE DIRECTION, ESTABLISHMENT OF A NEHEMIAH HOUSING OPPORTUNITY GRANT PROGRAM, AND FEDERAL SUPPORT FOR URBAN HOMESTEADING AND COMMUNITY DEVELOPMENT BLOCK GRANTS.

MANY OF US WHO ARE HOMEOWNERS MAY HAVE BEEN ASSISTED BY FEDERAL LOAN PROGRAMS. ALL OF US BENEFIT FROM THE FEDERAL TAX DEDUCTIONS SPECIFICALLY PLACED IN THE TAX CODE TO ENCOURAGE HOMEOWNERSHIP. WE CANNOT IN GOOD CONSCIENCE NOW SLAM THE DOOR ON FIRST-TIME HOMEBUYERS BY ENDING REVENUE BONDS, CURTAILING FEDERAL INSURANCE PROGRAMS, AND UNDERFUNDING COMMUNITY-BASED PROGRAMS THAT ASSIST THEM.

I CANNOT STRESS TOO STRONGLY THAT THE FEDERAL GOVERNMENT CANNOT TURN OVER HOUSING RESPONSIBILITY TO THE STATES AND AT THE SAME TIME CONTINUE TO REMOVE THE TOOLS WE MUST HAVE TO CARRY OUT THOSE RESPONSIBILITIES.

THANK YOU.

TESTIMONY OF OREST T. DUBNO
EXECUTIVE DIRECTOR, CONNECTICUT HOUSING FINANCE AUTHORITY
BEFORE THE HOUSING AND URBAN AFFAIRS SUBCOMMITTEE
OF THE SENATE BANKING COMMITTEE
JULY 1, 1987

Introduction

Mr. Chairman and Members of the Committee, my name is Orest T. Dubno and I am the Executive Director of the Connecticut Housing Finance Authority (CHFA). CHFA is one of the oldest State Housing Finance Agencies in the nation, serving the people of the State of Connecticut for 18 years. During that time the Authority has financed the purchase of approximately 45,000 homes predominantly for first-time buyers, and the construction or substantial rehabilitation of over 13,000 rental units for low and moderate income families.

Today, housing issues are receiving widespread and serious attention in the State of Connecticut.

-Both the Governor and the State legislature have made housing a top priority. The Governor has been requesting record amounts of state funding for the homeless and the construction of affordable rental housing.

-The Connecticut Business and Industry Association and regional business associations such as the Southwest Area Commerce and Industry Association in Stamford are giving housing issues an unprecedented level of public attention. Businesses have expressed concern due to the difficulty some companies have had recruiting employees to relocate to Connecticut due to the high cost of housing, particularly in Fairfield County. Also, business is increasingly concerned that high housing costs could start to play a role in wage and salary demands. Local governments in Fairfield County have had difficulty recruiting teachers in this part of the state to support the quality education that the people of our state demand.

Association in Stamford are giving housing issues an unprecedented level of public attention. Businesses have expressed concern due to the difficulty some companies have had recruiting employees to relocate to Connecticut due to the high cost of housing, particularly in Fairfield County. Also, business is increasingly concerned that high housing costs could start to play a role in wage and salary demands. Local governments in Fairfield County have had difficulty recruiting teachers in this part of the state to support the quality education that the people of our state demand.

-Regional associations of local governments have been studying local housing issues to provide state and local government leaders with valuable information.

I would like to share with you some observations regarding one aspect of a group of issues which comprise the "housing crisis" as it is commonly referred to in Connecticut- the problems faced by first-time homebuyers and what CHFA has been doing recently to address these issues.

Housing Problems are Interrelated

I would like to preface my comments by noting that is very important that the sub-issues that constitute the "housing crisis" be seen as related to one another. Too often concentration on the particular problems of one or another special sector of the population having difficulty securing safe, decent and affordable housing hides some "larger truths" about the manner in which the problems of these particular sub-groups are common and related to each other.

Approaching the problems of the first-time-homebuyer is a good example of the "interrelatedness" of housing issues. These purchasers are the bridge between the rental and homeownership markets. When young individuals and families are unable to purchase their first homes due to the unavailability of sufficient homes at prices they can afford, a number of situations can arise.

-Household formation or the bearing of children is delayed.

-Individuals and families are forced to rent longer with higher incomes enabling the market for rental housing to attain higher rents- to the detriment of lower income families.

-The market will seek to provide for their homeownership needs through the conversion of existing rental stock to condominium ownership- also often to the detriment of the lower income renter by increasing the rents in the remaining rental stock.

In Connecticut, we can see evidence of these dynamics at work. The problems of young homebuyers and renters are related in that they are both seeking to make use of a housing stock that is not growing sufficient enough to meet their collective demand.

The overall supply of new homes needs to be increased to meet demand, and participation in the market needs to be broadened. Adding supply in the areas of affordable moderate and low-income rental housing and housing suitable for first-time buyers is important. We must realize that a large degree of the dynamics of the production of affordable housing is beyond the influence of CHFA and the Congress. Many of the important details determining whether or not we have affordable housing production for homeownership lie in the thousands of decisions that are made every day by countless state and local governments. This is one area in which all levels of government and the private sector must work together to seriously address the issue. CHFA is eager to do all that it can to raise resources to finance the solution to the problem, to serve as a friendly, patient and active credit facility. We hope that over the next two years we can develop new mechanisms for the state to work even more intensively with the Federal and local levels.

The Connecticut Situation

In many ways the current housing environment in Connecticut is one of paradox. With strong economic expansion, one of the lowest unemployment rates in the nation, and the highest per capita income in the United States our overall economic condition is the envy of many.

However, these general conditions mask some vexing local and regional difficulties. Trends in income level and growth vary widely across the State, from Fairfield County to the rural Windham in the Northeast corner. While Connecticut contains some of the wealthiest communities in the country, it also contains some of the poorest local neighborhoods in the Northeast.

A number of general demographic factors have made for a very strong housing market in Connecticut. The State's population continues to grow though at slower rates than in the 1960's and 1970's. The 1970 to 1980 population growth was 2.5 percent, but with an increase in households of 17 percent from 933,269 to 1,093,678 and a decrease in household size from 3.16 persons per household in 1970 to 2.76 persons in 1980. The number of persons in the 25 to 34 age group, the age of household formation and home purchase, has been increasing in recent years and is anticipated to increase another 15 percent before gradually tapering off in the early 1990's. The number of elderly persons has also been increasing. People are living independently longer in their own homes, postponing the date when their home would be turned over to a younger generation of homebuyers. The drop in home mortgage rates and strong income growth due to a robust economy have been additional factors contributing to strong housing demand.

The creation of new housing, as measured by the number of new housing permits issued reached record levels in 1986, and the activity seems to be continuing in 1987. According to the Connecticut Department of Housing's 1985 and 1986 Annual Housing Market Reports, the number of units permitted for construction over the past three years has increased dramatically. The growth in the state totals by housing type are summarized in Table A.

Affordability Problems

The important questions which these raw data on new construction do not answer are:

-At what price are these units selling for ?

-If they are selling at prices affordable to first-time homebuyers are these units an adequate addition to the supply of affordable homes already in the market to meet the existing demand for homes affordable

TABLE A

New Housing Units Authorized for Construction in Connecticut

1984-1986

YEAR	1-detchd.	1-attchd	2	3&4	5 plus	TOTAL
1984	9,517	4,298	512	385	3,425	18,137
1985	12,463	5,025	622	490	6,141	24,741
1986	14,198	6,619	744	739	5,901	28,201
TOTAL	36,178	15,942	1,878	1,614	15,467	71,079

Source: Connecticut Department of Housing, Department of Housing Construction Activity Information System (DOHCAIS) as reported in DOH Annual Housing Market Report for 1985 and 1986.

to first-time homebuyers ?

Enough general data and anecdotal evidence has come to light over the past two years to provide a good guess as to the answers to these questions.

-The prices for these newly constructed homes appears to be well above that which could be afforded by typical first time homebuyers. Builders in Connecticut appear to be building for the more lucrative "trade-up" market while building comparatively little for the "first purchase" market.

-The supply of new or existing homes, particularly single-family detached homes, affordable to first-time buyers appears to be inadequate. Increases in the price of single-family detached homes and condominiums has been escalating at rates well beyond the rate of income growth or inflation.

Recent information on the typical costs of construction in Connecticut shows that newly-constructed homes are typically not being targeted for the first-time buyer.

The Home Builders Association of Connecticut has indicated that the cost of construction for a single family detached home in Connecticut rose substantially in 1986 over 1985. While the cost of financing, materials, and fees & permits rose slightly or even dropped, the cost of labor and land rose dramatically. This reflects the strong State economy and the degree to which the demand for land exceeds the available supply. A summary of the rise in costs of single family construction since 1983 in summarized in Table B.

An average of ten percent profit on sale would yield a price of sale for the

TABLE B

Changes in Construction Cost Components

For New Single Family Homes in Connecticut 1983 to 1986

	Costs 1985	Costs 1986	%Chng. 83-84	%Chng. 84-85	%Chng. 85-86
Land	$30,470	$48,500	11.7%	10.0%	59.2%
Labor On-Site	$16,050	$18,475	10.5%	20.0%	15.0%
Materials	$25,175	$26,182	4.2%	6.0%	4.0%
Financing	$9,542	$9,500	4.9%	-1.0%	-0.4%
Fees/ Permits Etc	$7,788	$8,010	1.3%	2.5%	2.9%
Overhead/ Profit	$8,030	$9,234	5.8%	10.0%	15.0%
TOTAL	$97,055	$119,883	7.3%	7.5%	23.5%

Source: 1986 Annual Housing Market Report, Connecticut Department of Housing, March, 1986.

buyer of $131,871, well beyond the reach of the most first-time buyers.

There are a variety of sources of data on actual sales prices of single family homes, generally agreed to be structures of 1 to 4 units. Though there is variation in the manner in which the data is represented and what it purports to indicate, all of the available data shows strong increases in home purchase prices over 1985-1986, ranging as high as 20 to 30 percent over that period in many of Connecticut's major housing markets.

These trends are particulary prevalent in Fairfield, Hartford and New Haven Counties. In these areas the average or median purchase price for a single family home is beyond the purchasing power of the young households with close to median income.

In its report " Affordable Housing: A Growing Crisis" the Connecticut Business and Industry Association states:

> "As median family incomes have failed to keep pace with price increases for housing, families have seen a growing "affordability gap". Between 1940 and 1979, increases in disposable income more than offset increases in housing costs. This positive relationship came to an abrupt end in 1979, when, for the first time since 1953, the median income family could not afford the purchase of a median-priced home. By 1983 this gap had grown to a point where the median-priced home was $16,000 too expensive for the median-income family...Obviously, recent declines in rates for 30-year mortgages which have dropped to 10 percent and lower have eased this gap, but subsequent price increases have offset these gains. Thus the affordability gap continues to widen as housing becomes more expensive."

Our recent observations have certainly found no evidence to contradict this statement. According to the Capitol Region Council of Governments, in the Hartford area, which for many economic indicators is the rough median for the state, the median sales price for a single family detached home in 1986 was about $116,000. In 1985, the comparable price was about $93,000, making the annual increase that year about 24 percent. Income estimates provided by the Census Bureau and the Department of Housing and Urban Development for the same general period equals about 10 percent, clearly indicating a widening affordability gap.

Condominiums

There has been an increase in the number of condomiums brought into the market to provide a more affordable form of homeownership for families that have very little chance of purchasing more expensive forms of housing. Condominiums can be added to the market either through the conversion of ownership tenure in existing buildings from general rental to individual unit ownership or through the construction of multiple unit structures intended for individual unit owners. The former may provide additional homeownership possibilities for young families, but has the negative effect of taking roughly the same number of rental units out of the rental markets. The latter is more positive and preferable since affordable homeownership is provided by adding to current supply.

Accurate and complete information on condominium ownership and development is difficult to obtain. The 1980 Census of Housing lists a total of 33,222 condominium units in Connecticut, or about 5.5 percent of the total housing stock. According to annual information collected by the Connecticut Department of Housing indicates that 11,502 condominiums were added to the homeownership stock through conversions from 1981 through 1986.

Recently, CHFA conducted a rental market survey of over 28,000 rental units in Connecticut. Though this survey was done primarily to gather market information for the purpose of underwriting multifamily rental housing loans, it did reveal some very interesting information on the pattern of condominium conversion within the state. From June of 1985 to January of 1987 our survey indicated that 3,127, or 11 percent, of the 28,443 units surveyed had been converted to condominiums. This problem was found to be particularly prevalent in Fairfield County where the percentage of units converted was two to four times the percentage of all units surveyed. In Stamford 26 percent of the units had been converted, in Bridgeport 38 percent and in Danbury 48 percent or nearly half of all the rental units surveyed had been converted from rental housing to condominiums.

Determining the amount of newly constructed condominiums that have been added to the market during this period is difficult to determine. In 1984 the Scott-Fitton Company of New Haven estimated in 1984 that there were approximately 65,000 condominium units in Connecticut and recently they estimated that there were about 5,600 condominium units constructed in Connecticut in 1986 alone. This represents a sizeable portion of all units that were other than single detached. However, it cannot be assumed that all of these condominiums were affordable for first-time buyers, and many of the new construction brought to the market is targeted to the market value in that area. Many new and existing condminium units in suburban Hartford and Fairfield County are well beyond the reach of the first-time buyers, being affordable only to the relatively affluent first-time buyer or as a trade-up purchase from a more modest detached home or condominium. Condominiums most affordable to first-time buyers tend to be those converted to condominium ownership from multifamily rental housing.

For Example: Detached Home

The difficulties facing homebuyers of moderate income and the advantages that CHFA's Home Mortgage Program brings to the moderate income first time homebuyer in this scenario can be illustrated by examining a purchase of a median priced home in the Hartford area by a young family comprised of 2 adults and a child. For the sake of illustration we will employ the 1986 median sales price for a single family detached home of $116,000, noting that this price is below median for 1987 and that it would be rare to find a home at this price in most of Hartford's immediate or secondary suburbs. A fixed mortgage interest rate of 10.5 percent, down payment of 10 percent and a privately insured mortgage are rough estimates of comparable instruments that are now available.

Under these assumptions our family of three cannot afford the purchase of a median priced home in the Hartford Area with only 10 percent down even though this amount of downpayment brings the anticipated cash to closing requirement up to only an estimated $13,600. In order to bring the mortgage amount for this purchase to a qualifying level for private mortgage insurance the downpayment would need to rise from $11,600 to $47,984. Our proposed buyer, at median income for a family of three is able to carry a mortgage of only about $68,000 on this purchase. In order to carrying a qualifying mortgage with a 10 percent downpayment our proposed purchaser household needs to have a qualifying income of just over $49,000 annually, more than $14,000 over their current income. Estimated median income for the Hartford area in 1987 is $38,800.

Assuming a CHFA Growing Equity Home Mortgage with an annual rate of 8 percent, our proposed purchaser is still considerably short of being able to carrying a qualifying mortgage with only 10 percent down. In order to obtain a qualified mortgage our purchaser would need to provide a downpayment of just over $31,000. While still considerably short of affordability on required cash for closing the CHFA mortgage did reduce this requirement by almost 35 percent.

For Example: A Condominium

The Capitol Region Council of Governments has reported that the median sales price for a condominium in the Hartford Area in 1986 was $77,000. Our household income of $34,920 at a mortgage interest rate of 10.5 percent and private mortgage insurance would barely qualify to purchase a condominiumn at this price with 10 percent down and a total of approximately $9,400 required at closing.

At the present time it is highly unlikely that any newly constructed condominiums could be found in the Hartford Area for this price. Typically, a unit of this price would be in a structure converted from rental housing to condominium ownership. Additionally, the coverage for FHA insurance for condominium purchase is less than universal. No purchaser other than previous tenants may purchase a unit with FHA insurance during the first year of sale. Also, since many owners and associations have had little difficulty in marketing their units in a strong market without FHA insurance there is little incentive to take the minimal time necessary to compete the paperwork

required to qualify the development for FHA insurance.

FHA Insurance

A substantial portion of CHFA mortgagors have traditionally obtained their mortgage insurance through FHA. Since January of 1985, FHA has insured about 60 percent of the mortgages financed by the Authority. Therefore, it is useful to examine each of our proposed loans in light of FHA underwriting standards. This program does serve to make the homes that are available more affordable for the first-time homebuyer using CHFA's Home Mortgage Program. Its residual income method of underwriting allows the prospective first-time buyer to carry a larger mortgage and thereby make it possible for the buyer to enter the market.

The usefulness of FHA insurance for many in Connecticut is limited by the $90,000 maximum mortgage amount established nationally for high cost areas. Often first time buyers are eligible under FHA underwriting standards to carry the necessary mortgage on their desired purchase but are unable to raise the necessary cash to make up the difference between the mortgage maximum and the actual sales price. Our local FHA office has noted to us that their business is down substantially despite increasing institutional interest and enthusiasm from major banks in the state that have traditionally not been as interested in FHA programs. The concensus seems to point to the mortgage maximum as to the reason for the fall-off in FHA activity in Connecticut.

Our sample purchase provides a good illustration. By using FHA mortgage insurance underwriting criteria and a 10.5 percent 30-year fixed rate mortgage our family of three can now afford to carry a mortgage of $110,000, giving this purchase a 95 percent loan-to-value ratio, with total closing costs estimated to be about $8,000- dramatically reducing the "cash to closing" requirement.

However, since FHA insurance will allow only a $90,000 mortgage in the Hartford area, this purchase would require a down payment of $26,000, giving this purchase a 78 percent loan-to-value. Therefore, while the purchaser remains qualified for a much larger mortgage, the cash required for closing is at a level that is typically prohibitive for many first-time homebuyers. With reference to the more advantageous terms offered through a CHFA mortgage, currently at 8.0-percent compared to 10.5, a borrower of even more modest means could qualify for this home purchase but would face the same cash requirements.

This cash-to-closing requirement could be met by very few families without approved second mortgages, assistance from other family members in the form of a gift or an extended deferement of purchase in order to save the required downpayment. This last alternative is problematic in Connecticut at this time due to the rapid escalation in prices, often well ahead of income growth or ability to save due to relatively high rent levels.

Our proposed condominioum purchase easily fits within FHA program guidelines. Should this condominium be eligible for FHA insurance our household would easily qualify for this purchase. In fact, with FHA insurance and a minium downpayment of $3,350, a household with even less income would qualify for the purchase.

CHFA's Present Role

In the past two years, despite the extensive damage done to our programs by the Tax Reform Act of 1986, CHFA has continued to play an active role in Connecticut assisting first-time homebuyers through our standard Growing Equity Home Mortgage Program which remains active, and a Pilot Construction Program for Low Income Homeownership for which all funds have been committed.

The Growing Equity Home Mortgage Program is CHFA's primary homeownership assistance program for eligible low and moderate income households. Through the sale of bonds CHFA is able to provide mortgage loans at fixed rates often as much as 200 basis points below prevailing competitve instruments. In this program the initial payment is based on a 30 year amortization schedule with an increase in monthly payments effective every two years equal to 60¢ per $1000 borrowed. This increase is applied entirely against principal, thereby constituting a gradual prepayment of the mortgage, which is retired in 17 years rather than 30. This reduces the time that homeowner is required to carry a mortgage and reduces the tax loss to the Federal Treasury since significantly less interest is deducted from the borrower's income over the amortization period. All loans are insured either by FHA, VA or a private mortgage insurance company. The purchases financed by this program must meet mortgagor eligibility standards and home purchase price standards established by Federal law. Additionally, CHFA's Home Mortgage Program has long operated under state-initiated policies that have called for sales price and income limits lower that those prescribed by Federal law and provided special incentives for purchases in targeted urban areas.

Historically, CHFA has set aside a certain percentage of available funds for the purchase of newly constructed homes. These funds, typically about 25 percent of the funds made available were reserved for the individual purchasers on a statewide basis for a given number of months. Should the funds not be used during this period, they would be freed for commitment to purchasers of existing housing. CHFA assumed this practice when demands for home mortgage funds for purchasers eligible for our program was high and it was possible that the funds would be expended in a short period of time to the purchase of existing homes. With the recent escalation in home prices, and the difficulty facing first-time purchasers in finding home to purchase, CHFA has found that funds have generally been available on an ongoing basis for the purchase of new and existing homes thereby negating the need to set aside funds for newly constructed home.

Since January 1, 1985, CHFA has issued a total of $478,000,000 in securities to finance home mortgage through the Home Mortgage Loan Program. In 1985, $225,000,000 in bonds was issued prior to the Tax Reform Act of 1986. The remaining issues have been taken to market by CHFA as "Current Refunding" bonds not subject to the volume and program restrictions of the Act. If not for Current Refunding bonds, the amount of funds available for homeownership programs in Connecticut would have been significantly lower. In the absence of Tax Reform CHFA would have been eligible to issue an additional $225,000,000 in bonds for this program over the past two years.

Loan transactions since January 1, 1985 which have closed to date total 6,022 mortgages with 5,715, or 95 percent financing purchases by first time homebuyers. The average purchase price was $70,710, a loan of $62,488 leaving a downpayment of $8,373. The average purchasing household had an income of

$27,169, 7[illegible].4 percent of the average statewide median during this period of $36,500. The average borrower age of was 31 years, with 2 or 3 persons in the household and one person working. Of these loans 1,405 have been for newly constructed homes, and 3,721 have been insured by FHA.

The purchasers using CHFA programs have always been of comparative modest means and purchased moderately priced homes. While this trend has been maintained over the past two years our program has not been immune from market conditions in the state generally. Since January 1, 1985 the profile of the average CHFA financed purchase has changed is summarized in Table C.

The Pilot Single-Family Construction Loan Program was initiated by CHFA to provide homeownership opportunities for households making less than $23,000 annually. In order to achieve this objective CHFA made available both construction financing for non-profit and "for-profit" developers to construct the homes and the permanent financing for the eventual eligible purchasers of the units. Permanent mortgage loans were made available to purchasers at interest rates as low a 4 percent in order to make the purchase affordable to lower income families. State Department of Housing Downpayment Assistance was made available for eligible mortgagors, enabling low income purchasers to obtain 100 percent financing as long they were able to carry the debt under FHA or VA standards. All of the $15 million made available for this program has been committed. We are presently reviewing our experience with this program, and exploring broader application of the concept.

Both of these CHFA programs have been used in conjunction with the Downpayment Assistance Program offered by the Connecticut State Department of Housing. This program exclusively assists first-time homebuyers using CHFA's

TABLE C

Changes in Average CHFA Mortgagor & Purchase

1985-1987

	Purchase Price	Mortgage	Down Payment	Mortgagor Income
1985	$63,725	$56,269	$7,793	$26,620
1986	$74,495	$65,788	$8,561	$26,466
1987	$87,861	$77,941	$10,118	$30,004
% Chng. 1985-87	+37.8%	+38.5%	+29.8%	+12.7%

homeownership program. On an uninsured basis a borrower can obtain up to 25 percent of the acquisition cost of a home for a period of thirty years at an interest rate of 6 percent. Condominiums approved by CHFA are eligible. The program is accepted by both FHA and VA in Connecticut as long as the the borrower can carry both mortgages under the applicable underwriting criteria. This program has been a valuable tool for the Authority since sales prices have escalated beyond FHA's mortagage maximum. Currently, about one-third of our single family mortgages are being committed in conjunction through this cooperative effort. In the current state fiscal year $2,000,000 was provided to fund this program, and the possibility remains that additional funds will be made available for this program this year when the original allocation is depleted.

Summary

The prospects for homeownership for households that have traditionally been in the market for their first home purchase has become more difficult in recent years in Connecticut. The excess of demand for "starter homes" homes on detached lots greatly exceeds the supply pushing the price for these homes to a level that only the most affluent of these households can afford. Condominium ownership provides an affordable alternative to many. However, the prices of many of these units are beginning to escalate beyond the reach of many first-time buyers. The most affordable homeownership alternative for many first-time purchasers is in multi-family structures that were previously rental housing. This places the demands of first-time buyers in direct conflict with the need to maintain an adequate supply of affordable rental housing for those renters that are trying to save for their first home purchase and those

Senator **Cranston**. Thank you a great, great deal, and thank you for sticking to our 5 minutes and even doing better. I appreciate that because we have a long agenda.

Senator Graham of Florida will introduce our next witness.

Bob, welcome.

Senator **Graham**. Thank you, Mr. Chairman.

Mr. Chairman, while I was Governor of Florida one of my proudest moments was the passage of the constitutional amendment to authorize the establishment of the State Housing Finance Agency, which we recognized as an urgent need and a great administrative challenge to bring leadership that would justify the optimism which has been invested in that new initiative.

Florida was extremely fortunate to find such leadership in Mark Hendrickson. Mark came to our State after a distinguished career in Arkansas, where he had headed that State's Housing Development Agency. From 1981 to the present, he has provided the direction in Florida's Housing Finance Agency, which came from its infancy to be one of the largest agencies in the Nation during his period of direction.

I am very proud of the association that I have had both governmentally and personally with Mark Hendrickson, and I am confident that he will provide the same type of leadership to national housing direction that he has done so forcefully and effectively within our State.

Senator **Cranston**. Thank you, Bob.

After that introduction, we expect you to tell us how to solve all our problems. [Laughter.]

STATEMENT OF MARK HENDRICKSON, EXECUTIVE DIRECTOR, FLORIDA HOUSING FINANCE AGENCY, TALLAHASSEE, FL

Mr. **Hendrickson**. Thank you, Senator Graham, for that kind introduction, and thank you, Mr. Chairman, for this opportunity.

After that, everything I had to say people have already said. So maybe I don't have as much to say right now as I had prepared coming in here.

But I think that there are some points that need to be reemphasized, and I don't think we can say them enough in terms of what the problems are and what some of the solutions have to be at both the Federal and the State level. The previous speakers have alluded to them, but I wanted to touch base on some of these problems again.

The first is the cost of housing versus income. One of the earlier speakers stated that it is not just a problem in high cost areas; it is a problem in places like Florida, which has moderate costs, and it is a problem in places like Arkansas, which have very low costs.

The problem is the gap between the rise in income and the rise in housing prices. So if you go to rural Florida where housing costs are very low compared to California or New York, you still have an affordability problem and people have trouble getting into that first home.

Some of the reasons that compound that problem relate to rental housing production. If people are paying too much of their income for rent, they are never going to accumulate the savings that they need to put down that down payment and to pay the closing costs.

We have found that we have home buyers or potential home buyers who want to get into our homeownership program that are living in rental developments that we have financed, and they have called up and said, "I am being turned down for this home loan. What is the problem? If I move into the house, my payment is going to be $500 a month, and I am right now paying $550 or $600 a month in rent. It is obvious that if I can pay $600 I can pay $500 and be in homeownership."

But what we find is that they don't have enough capital up front to qualify and because of increasingly strict mortgage insurance credit underwriting standards, it is increasingly difficult to get the first-time home buyer qualified for the mortgage insurance that is necessary to have a loan that is salable on the secondary market.

So that the lack of rental production is a problem, the insurance premiums and the insurance credit underwriting standards are a problem, and the overall necessity for more and more cash from people that have trouble accumulating cash is a major problem.

One of the things that we have found—when I was preparing this testimony—is that the change in the mortgage insurance credit on underwriting standards, the debt-to-income ratios that they will allow have decreased over the past 6 years in a way that have an impact as if interest rates had gone up 3 percent.

In other words, they used to allow someone to have 33 percent of their income to go to a housing payment, it is now 25 percent; in terms of qualifying for a home loan that is the same as if you just raised their interest rate 3 percent. It is as if a lot of the downturn in interest rates over the past 5 years have been offset in terms of qualifying first-time home buyers by those changing mortgage insurance standards.

Without FHA insurance, the State of Florida's Housing Finance Agency would have made almost no loans to first-time home buyers in the past 2 years. So to again repeat, it is critical that the FHA insurance program be continued, and hand in hand with that, without mortgage revenue bonds first-time home buyers would be in very much greater difficulty.

So I again emphasize the need for the continued mortgage revenue bond program beyond its sunset at the end of 1988.

One other thing that I wanted to touch base on in terms of the State of Florida, we have the city of Key West, which has become—it is sort of a microcosm for the future of Florida. We have talked about that many times in the growth management. It is an area that there is limited land to develop, there is a lot of development regulations, and we just did a market study on what could our agency do for the city—for housing in Key West for moderate income persons, and what that study came back with was that it told us that there wasn't a whole lot that we as the Housing Finance Agency could do in that situation and certainly very little by ourselves.

That was discouraging, and probably the most discouraging thing that came out of that is that the report recommended to us that we work with the industry and the employers in Key West to try to encourage them to build industry owned dormitory style housing for workers.

And I think if that's the best that we have for the moderate-income family in the future, is dormitory style housing, that's not a very favorable future.

So I think that there are things that the Federal Government in conjunction with State government can do—continue FHA insurance, continue mortgage revenue bonds, but we need to work together to come up with a method to help people with their cash requirements up front, ways to help them offset or source for them to come up with the money for the down payment.

Thank you, Mr. Chairman.

[The complete prepared statement of Mark A. Hendrickson follows:]

who may never choose or be able to afford homeownership.

In order to provide more affordable homeownership opportunities for renters and broaden the market participation of first-time buyers.in Connecticut the supply of both types of housing needs to increase. Government at all levels and the private sector must work together to seriously address the issue. Again, CHFA is eager to do all that it can to raise resources to finance the solution to the problem. I would therefore make three basic suggestions as to actions that this Committee could undertake in order to assist CHFA in providing greatly needed affordable homeownership in Connecticut:

-SUPPORT THE PASSAGE OF LEGISLATION EXTENDING THE SUNSET DATE FOR THE MORTGAGE REVENUE BOND PROGRAM FOR ANOTHER FOUR YEARS AND ENSURE THAT CURRENT REFUNDING BONDS REMAIN AVAILABLE PERMANENTLY TO FINANCE HOMEOWNERSHIP PROGRAMS;

-AND FREE BOTH MULTI-FAMILY AND SINGLE FAMILY HOUSING BONDS FROM THE CURRENT OVERALL LIMITATION ON STATE AND LOCAL PRIVATE ACTIVITY DEBT, PLACING THESE PROGRAM UNDER A SEPARATE HOUSING CAP AT PRE-TAX REFORM LEVELS OF ACTIVITY ADJUSTED FOR INFLATION.

-SUPPORT THE DEVELOPMENT OF WORKABLE AND EFFECTIVE EQUITY INCENTIVES TO ENCOURAGE THE DEVELOPMENT OF AFFORDABLE RENTAL HOUSING, EVEN IF IT IS NOT STRICTLY FOR LOW INCOME PERSONS.

Also, in the Tax Reform Act of 1986, the Congress made several changes with regard to eligibility standards for homeownership and rental programs that have

significantly reduced the flexibility of state HFA's in establishing their own programs tailored to local housing market conditions. For example it may prove to have been unnecessary and a mistake to set a Federal income standard for homeownership programs financed with MRB's in addition to the sales price limits already in force, since purchase price does generally limit income by proxy according to local market conditions. Adding HUD estimates of income to the equation increases complication without necessarily attaining added "public purpose" benefits.

Many of these requirements have been unnecessary, and the same public policy objectives could have been met if different more flexible systems had been insituted. An increasing sensitivity, and an assumption of good faith, on the part of the Congress in redressing these issues and designing standards for new initiatives would be greatly appreciated.

The CHFA remains a strong and enthusiastic supporter of FHA single-family insurance programs. Congress should look closely at ways to make this program more broadly applicable in high cost areas, for those mortgagors who would not be eligible for state HFA homeownership programs. We strongly support the increase in the FHA maximum mortgage amount from the current maximum of $90,000 to $101,250 in high cost areas. However, though this increase is a positive for Connecticut and welcomed, a more flexible system reflecting actual market conditions in the states should be considered. The Mortgage Banker's Association has made, and I would support, suggestions for such a system.

TESTIMONY OF THE
FLORIDA HOUSING FINANCE AGENCY
BEFORE
HOUSING SUBCOMMITTEE OF THE
SENATE BANKING COMMITTEE

Delivered By Mark A. Hendrickson
Executive Director
Florida Housing Finance Agency

MR. CHAIRMAN, MEMBERS OF THE COMMITTEE, MY NAME IS MARK HENDRICKSON, AND I REPRESENT THE FLORIDA HOUSING FINANCE AGENCY (FHFA). I HAVE SERVED AS EXECUTIVE DIRECTOR OF FHFA FOR THE PAST SIX YEARS, AND SERVED IN THE SAME CAPACITY FOR ARKANSAS'S HOUSING FINANCE AGENCY FROM 1978-1981. OVER THE PAST TEN YEARS, I HAVE WITNESSED AN ALARMING DROP IN THE AFFORDABILITY OF HOUSING, PARTICULARLY FOR LOW AND MODERATE INCOME FIRST-TIME HOMEBUYERS. THIS TESTIMONY WILL FOCUS ON THE DECLINING AFFORDABILITY OF HOMEOWNERSHIP IN FLORIDA, AND WILL ATTEMPT TO POINT OUT SOME OF THE LESS OBVIOUS CAUSES OF THE PROBLEM.

BACKGROUND ON HOUSING AFFORDABILITY PROBLEM IN FLORIDA

THE DEMAND FOR AFFORDABLE HOUSING IN FLORIDA HAS BEGUN TO OUTSTRIP THE AVAILABLE SUPPLY. AT A RATE FOUR TIMES THAT OF THE NATION AS A WHOLE, POPULATION GROWTH IN FLORIDA HAS HAD A SERIOUS IMPACT ON HOUSING, AFFECTING BOTH AVAILABILITY AND AFFORDABILITY. THE PERCENTAGE OF FLORIDIANS THAT CAN AFFORD TO PURCHASE OR RENT SAFE AND SANITARY HOUSING HAS DECLINED PRECIPITOUSLY IN THE LAST TEN YEARS --- FOLLOWING RATHER SIGNIFICANT PROGRESS MADE IN THE 1960'S AND EARLY 1970's. HOUSING COSTS HAVE RISEN SHARPLY, WHEREAS INCOME HAS INCREASED AT A SLOWER PACE.

HARDEST HIT ARE THE LOW AND MODERATE INCOME FAMILIES THAT MUST PAY A PROHIBITIVELY HIGH PORTION OF THEIR INCOMES FOR RENT. SUBSEQUENTLY, THEY ARE UNABLE TO SAVE SUFFICIENT FUNDS TO COVER THE UPFRONT COSTS OF HOMEOWNERSHIP, AND ARE OFTEN UNABLE TO MEET THE INCREASINGLY STRICT CREDIT UNDERWRITING STANDARDS OF PRIVATE MORTGAGE INSURANCE COMPANIES. VERY LOW INCOME FAMILIES HAVE SUCH LIMITED RESOURCES SO AS TO MAKE HOMEOWNERSHIP IMPRACTICAL WITHOUT MASSIVE, COST INEFFECTIVE SUBSIDIES.

THIS CURRENT PROBLEM OF HOME OWNERSHIP AFFORDABILITY IN FLORIDA IS THE RESULT OF (i) THE RISING COSTS OF LAND, CONSTRUCTION AND FINANCING (ii) AN EXTREME REDUCTION IN FEDERAL FUNDING FOR RENTAL HOUSING (iii) STRICTER CREDIT UNDERWRITING STANDARDS, AND (iv) ADDED LAND USE RESTRICTIONS COUPLED WITH PHENOMENAL GROWTH. THESE FACTORS COMBINED HAVE RAISED THE COST OF HOMEOWNERSHIP TO A LEVEL THAT IS NO LONGER AFFORDABLE FOR MANY FLORIDIANS.

MANY OF THE CAUSES OF THE HOMEOWNERSHIP PROBLEM ARE CLEAR, SUCH AS INCREASED LAND AND CONSTRUCTION COSTS, AND THE IMPACT OF RISING MORTGAGE RATES. THE FOLLOWING SECTIONS WILL ELABORATE ON LESS WELL KNOWN CAUSES, INCLUDING THE (i) LACK OF AFFORDABLE RENTAL HOUSING, (ii) STRICTER CREDIT UNDERWRITING STANDARDS AND

HIGHER COSTS OF MORTGAGE INSURANCE, AND (iii) THE IMPACT OF LAND USE RESTRICTIONS ASSOCIATED WITH EFFECTIVE GROWTH MANAGEMENT.

LACK OF AFFORDABLE RENTAL HOUSING

THE FLORIDA HOUSING FINANCE AGENCY (FHFA) AND THE FLORIDA DEPARTMENT OF COMMUNITY AFFAIRS ESTIMATE THAT OVER TWO MILLION RESIDENTS ARE EXPERIENCING CRITICAL HOUSING PROBLEMS, MEANING THAT THEY ARE PAYING A DISPROPORTIONATE SHARE OF THEIR INCOME FOR HOUSING, OR THAT THEY ARE LIVING IN SUBSTANDARD CONDITIONS. IT IS ALSO ESTIMATED THAT 84 PERCENT OF THE LOW INCOME HOUSEHOLDS IN FLORIDA SPEND OVER 30 PERCENT OF THEIR INCOME ON HOUSING. AN ADDITIONAL 35,000 UNITS MUST BE BUILT EACH YEAR FOR THE NEXT FIVE YEARS TO MEET THE DEMAND FOR AFFORDABLE MODERATE INCOME RENTAL HOUSING CAUSED BY POPULATION GROWTH. FAILURE TO PROVIDE ADEQUATE AFFORDABLE RENTAL HOUSING MAKES IT EXCEEDINGLY DIFFICULT FOR FIRST-TIME HOMEBUYERS TO SAVE SUFFICIENT FUNDS FOR A DOWNPAYMENT AND OTHER CLOSING COSTS.

AS FAMILIES THAT PREVIOUSLY WOULD HAVE BOUGHT THEIR FIRST HOME ARE REMAINING IN RENTAL HOUSING, THEY CREATE ADDITIONAL PRESSURE ON THE MARKET RESULTING IN INCREASED RENTS AND SHORTAGES OF AFFORDABLE UNITS. THIS CYCLE MUST BE BROKEN, PARTICULARLY BY THE PRODUCTION OF NEW RENTAL HOUSING TARGETED TO THE MODERATE INCOME FAMILY, WITH THE UNITS SERVING AS A TEMPORARY RESIDENCE ON THE ROAD TO HOMEOWNERSHIP.

FEDERAL CUTBACKS OVER THE LAST SIX YEARS HAVE VIRTUALLY ELIMINATED THE PRODUCTION OF NEW LOW-INCOME RENTAL HOUSING. THE TAX REFORM ACT OF 1986 SIGNIFICANTLY INCREASED THE VERY LOW INCOME TARGETING REQUIREMENTS IMPOSED ON BOND FINANCED RENTAL PROJECTS, WHILE REDUCING OTHER TAX CODE INCENTIVES FOR HOUSING PRODUCTION. THIS HAS EFFECTIVELY STOPPED THE PRODUCTION OF NEW MODERATE INCOME RENTAL HOUSING IN FLORIDA AND THE NATION. IN 1985, THE FHFA FINANCED 16,792 UNITS OF RENTAL HOUSING; IN 1986 AND 1987 COMBINED, ONLY 793 UNITS HAVE BEEN FINANCED, ALL "GRANDFATHERED" UNDER THE PRE-1986 INCOME TARGETING REQUIREMENTS. THIS LACK OF PRODUCTION WILL HAVE A SIGNIFICANT NEGATIVE IMPACT ON YOUNG FAMILIES ATTEMPTING TO SAVE THE FUNDS NECESSARY TO BUY THEIR FIRST HOME.

CREDIT UNDERWRITING STANDARDS

A REALITY OF TODAY'S MORTGAGE MARKET IS THAT LENDERS DO NOT MAKE AND HOLD MORTGAGES, BUT INSTEAD SELL THEM ON THE SECONDARY MARKET. A PREREQUISITE OF SUCH A SALE IS THAT THE MORTGAGES ARE INSURED TO THE SATISFACTION OF THE BUYER, AND THAT THE LOANS WERE MADE USING GENERALLY ACCEPTED CREDIT UNDERWRITING STANDARDS.

ALTHOUGH INTERST RATES HAVE DECLINED SIGNIFICANTLY IN THE LAST FIVE YEARS, STRICTER CREDIT UNDERWRITING STANDARDS HAVE ALL BUT ELIMINATED THE BENEFITS TO FIRST-TIME HOMEBUYERS OF THE LOWER

RATES. FOR EXAMPLE, SOME ELIGIBLE AND GENERALLY CREDIT WORTHY APPLICANTS TO THE FHFA'S FIRST-TIME HOMEBUYER LOAN PROGRAM ARE UNABLE TO PARTICIPATE IN THE LOAN PROGRAM DUE TO THE REQUIREMENTS THAT ARE NOW NEEDED TO CLOSE A LOAN. THE COST OF PRIVATE MORTGATE INSURANCE HAS RISEN MARKEDLY ALONG WITH THE MINIMUM REQUIRED DOWNPAYMENT. IN RESPONSE TO INCREASED FORECLOSURES, MORTGAGE INSURERS HAVE TIGHTENED THEIR UNDERWRITING STANDARDS; AS A RESULT, THE FIVE PERCENT DOWNPAYMENT CONVENTIONAL LOAN HAS EFFECTIVELY DISAPPEARED.

THE REDUCED DEBT TO INCOME RATIO THAT IS NOW ALLOWED HAS HAD AN EXTREMELY NEGATIVE IMPACT ON FIRST-TIME HOMEBUYERS. YOUNG FAMILIES ARE OFTEN MORE DEPENDENT ON CREDIT THAN THEY ONCE WERE. THEREFORE THE AVERAGE DEBT TO INCOME RATIO OF HOMEBUYERS IS HIGHER NOW THAN IT WAS TEN YEARS AGO. HOUSING COSTS HAVE ALSO RISEN AT A HIGHER RATE THAN REAL INCOME. AT THE SAME TIME, THE DEBT TO INCOME RATIO ALLOWED BY MORTGAGE INSURERS HAS DECREASED IN THE LAST FIVE YEARS FROM 33% MONTHLY/38% TOTAL DEBT, TO THE CURRENT RATIO OF 25%/33%. MANY FIRST-TIME HOMEBUYERS NO LONGER QUALIFY UNDER THE NEW GUIDELINES.

IN EFFECT, FIVE YEARS AGO A TYPICAL FIRST-TIME HOMEBUYER WITH AN ANNUAL INCOME OF $20,000 A YEAR COULD AFFORD A $44,000 MORTGAGE (13% MORTGAGE RATE). USING TODAY'S PRIVATE MORTGAGE INSURANCE UNDERWRITING GUIDELINES AND A 10% MORTGAGE RATE, THAT SAME FAMILY COULD STILL ONLY AFFORD A $44,000 MORTGAGE (WITH A LIKELY MINIMUM DOWNPAYMENT OF AT LEAST 10%, AS OPPOSED TO THE PREVIOUSLY AVAILABLE 5%). THEREFORE, THE BENEFITS OF THE SIGNIFICANT DROP IN INTEREST RATES HAVE BEEN NEGATED BY THE TIGHTER CREDIT UNDERWRITING STANDARDS.

GENERALLY, THE NEW STANDARDS RESTRICT THE PURCHASE OF INSURANCE TO INDIVIDUAL SAVINGS, ELIMINATING GIFTS AND FINANCIAL ASSISTANCE. ADDITIONALLY, THE HOMEOWNER MUST PROVE THAT THEY WILL STILL HAVE THE EQUIVALENT OF A MINIMUM OF TWO MONTHS IN HOUSING COSTS AFTER THE CLOSING. CONTRIBUTIONS SUCH AS BUILDER BUY-DOWNS ARE NOW LIMITED TO TWO PERCENT AND MUCH STRICTER DEFINITIONS OF EARNINGS ARE BEING APPLIED. ALL OF THESE FACTORS FURTHER INCREASE THE UP-FRONT CASH REQUIRED FROM THE BUYER.

CHANGES IN STANDARDS FOR INSURANCE ON CONDOMINIUM SALES HAVE HAD A DRAMATIC EFFECT IN FLORIDA. MORTGAGE INSURANCE COMPANIES GENERALLY WILL NO LONGER INSURE CONDOMINIUM LOANS WITH LESS THAN A 10 PERCENT DOWN PAYMENT. ON CONDOMINIUM CONSTRUCTION PROJECTS, THEY WILL ONLY RISK A 30 PERCENT EXPOSURE WHEREAS FIVE YEARS AGO THE AMOUNT WAS GENERALLY UNLIMITED. PRIOR TO THESE CHANGES CONDOMINIUMS WERE OFTEN THE LOWEST COST, MOST ATTRACTIVE OPTION FOR FIRST-TIME HOMEBUYERS IN THIS STATE.

THESE MORTGAGE INSURANCE RESTRICTIONS HAVE MADE IT INCREASINGLY DIFFICULT, IF NOT IMPOSSIBLE, FOR LENDERS TO MAKE LOANS TO MODERATE INCOME HOMEBUYERS WHICH CAN BE SOLD ON THE

SECONDARY MARKET. EVEN WITH THE AID OF BOND FINANCING, THE TASK IS DIFFICULT AS THE SUBSIDY IS IN THE FORM OF A LOWER INTEREST RATE, NOT REDUCED CREDIT STANDARDS. WITHOUT FHA MORTGAGE INSURANCE, THE FHFA WOULD HAVE MADE ALMOST NO LOANS TO FIRST-TIME HOMEBUYERS OVER THE LAST TWO YEARS.

GROWTH MANAGEMENT

FLORIDA'S ENORMOUS SURGE IN POPULATION HAS PROMPTED A NEW ENVIRONMENTAL AWARENESS AND CONCERN FOR MANAGING GROWTH THAT CULMINATED IN THE PASSAGE OF FAR REACHING GROWTH MANAGEMENT LAWS. THE OMNIBUS GROWTH MANAGEMENT ACT OF 1985 WAS SPECIFICALLY DRAFTED TO STRENGTHEN THE REQUIREMENT THAT ALL LAND DEVELOPMENT REGULATIONS AND ORDERS BE CONSISTENT WITH LOCAL COMPREHENSIVE PLANS. IT ALSO LIMITED LOCAL PLAN AMENDMENTS TO TWICE A YEAR AND GUARANTEED CITIZEN STANDING TO CHALLENGE SPECIFIC PLAN AND DEVELOPMENT REGULATION CONSISTENCY.

THE INTENT OF THE LEGISLATION, WAS TO STANDARDIZE DEVELOPMENT REGULATIONS TO BEST ACCOMODATE THE 300,000 OR MORE RESIDENTS THAT ANNUALLY MOVE TO FLORIDA, WHILE MAINTAINING THE STATE'S NATURAL BEAUTY AND INTEGRITY. ONE UNFORSEEN CONSEQUENCE MAY BE TO HINDER THE PRODUCTION OF AFFORDABLE HOUSING. AS MORE LAND IS PRESERVED, LESS LAND IS AVAILABLE FOR DEVELOPMENT. COMPETITION FOR THE REMAINING LAND INCREASES THE COST OF THAT LAND.

DEVELOPERS THROUGHOUT THE STATE HAVE MADE IT CLEAR THAT GROWTH MANAGEMENT CONTROLS, IN MANY INSTANCES, ENCOURAGE THEM TO DEVELOP LOWER DENSITY, HIGHER PRICED UNITS IN ORDER TO REALIZE A REASONABLE RETURN ON THEIR INVESTMENT. GROWTH MANAGEMENT REGULATIONS HAVE MADE IT MORE COSTLY TO DEVELOP. AS REPORTED BY THE H.U.D. FINAL REPORT OF THE TASK FORCE ON HOUSING COSTS:

> "... LOCAL GOVERNMENTS ARE STEADILY TRANSFERRING FROM THE COMMUNITY AT LARGE TO THE DEVELOPER, AND THENCE TO THE HOUSING CONSUMER, A GREATER SHARE OF THE PUBLIC CAPITAL COSTS OF GROWTH."

REGULATION IS COSTLY FOR A DEVELOPER: DELAYS IN CONSTRUCTION REQUIRE HIGHER CARRYING CHARGES, INCREASED TAXES AND PAYROLLS. THESE LOSSES MUST BE MADE UP ON EACH ONE OF THE UNITS THAT ARE BUILT. THE ADDITION OF IMPACT FEES, WHICH LOAD THE COST OF INFRASTRUCTURE DEVELOPMENT ON NEW HOUSING, COMPOUNDS THE AFFORDABILITY PROBLEM.

A MICROCOSM OF THIS AND THE ALL OTHER PROBLEMS DISCUSSED CAN BE SEEN IN KEY WEST, FLORIDA, WHICH HAS SIGNIFICANT LAND USE REGULATION AND A FINITE AMOUNT OF LAND AVAILABLE FOR DEVELOPMENT. A RECENT MARKET STUDY COMPLETED FOR THE FHFA CONCLUDED THAT THE AGENCY'S MORTGAGE SUBSIDY PROGRAMS COULD, BY THEMSELVES, HAVE NO SIGNIFICANT IMPACT IN STIMULATING RENTAL HOUSING PRODUCTION, LET ALONE AFFORDABLE OWNER-OCCUPIED RESIDENCES FOR YOUNG FAMILIES.

Senator CRANSTON. Thank you very, very much.

I'd like to pose just a few questions. And if one of you chooses to answer, you can decide among yourselves. Then, if anyone disagrees or has an amplification, please offer that.

Some of you have discussed the declining usefulness of FHA insurance in today's housing mortgage given the current mortgage limits.

The House and Senate passed housing bills, raised the FHA maximum mortgage limit in high-cost areas from the current level of $90,000 to $101,250.

Is that enough? And would you suggest any other changes?

Mr. HENDRICKSON. I think that that is certainly a very beneficial step. In speaking for this group, that limit has not been a major problem in Florida, but I know it's been a major problem in New York and Connecticut, Rhode Island, other areas, particularly in the Northeast.

One of the things that has considerably improved FHA—and I want to let you all know when something goes right—is the concept of delegated underwriting.

One of the problems that we had in using FHA insurance in the past is that it took too long to process the case at the FHA insurance office, and lenders and buyers would avoid FHA because it just took too long to get processed.

And over the past few years, the FHA has encouraged a program wherein the mortgage bankers can do the credit underwriting themselves and approve a case while they assume part of the risk of that credit underwriting.

That has significantly improved the usefulness of FHA for us in Florida.

Mr. DUBNO. I would just echo Mark's comments about allowing the participating lenders to do it and the limit obviously helps. In Connecticut, we were just able, when we received the Federal information, to raise our sales price limit from approximately an average of $110,000 to $134,000.

And certainly this increase to $101,000 would be very, very helpful. Making FHA permanent would also be very helpful and eliminate the uncertainties.

Senator CRANSTON. We passed legislation to do that in the Senate. Some people have argued that the Federal Government really has no role in alleviating the problem of housing affordability. The problem can be solved by local government and by private industry.

You've mentioned a number of things that the States and other local entities have done. What do you feel that the Federal Government's main role should be? Any innovative suggestions as to Federal efforts?

Mrs. CADE. I think we tried to mention some ideas as we spoke, what would clearly be the big ticket items—the ongoing rental housing support must be a Federal Government item because of the magnitude of that.

The programs I've described both in the insurance and in the mortgage funds from State funds are very, very important. But they are very small in comparison with the need.

When I say that we have a 4-percent mortgage program, there's still only maybe $10–$12 million a year to make available in that program; where through the taxes exempt revenue bonds, we were at one point having about $300 million go into single-family homeownership.

There needs still to be the sense that there is a Federal overall housing policy, so that people aren't crossing State lines to get a benefit of housing that exists in one State and not in another State.

Senator Cranston. Specifically, would you make any changes in the mortgage revenue bond program?

Mr. Hendrickson. I'll start on that.

Yes. Clearly, the income limit that was placed on mortgate revenue bonds last year at 115-percent median, we felt was an unnecessary restriction. What it has done in many areas is limit the program to people that have trouble affording a house even with the program. And there's a group that's right above that in the 115–130 a median that, in the past, has used the program, need the help, but they're locked out.

And, in fact, Senator, one of the things that we find is that the people that are penalized by that income limit are two-income households. If people motivate so that both the husband and the wife have a job, they may have entry level jobs that aren't particularly well-paying, but the two of them together will push them above that 115 percent limit. And they're in fact penalized for having gone out and increased their income.

Senator Cranston. Because of the Federal deficit, there are obviously problems on what we can do in terms of cost. But would you recommend that the Federal Government provide subsidies for down payments and other costs to qualify first-time home buyers?

Mrs. Cade. It seems that there must be some tool provided because, as we have found, the biggest barrier is getting over that hump of getting through the entry costs door and getting past the closing table.

Our figures in Annapolis, MD, where we have fairly high closing costs and, say, a 10-percent down payment, you'd have to come to the closing table with about $17,000 on a $100,000 house.

And it is really out of the reach of many people who are even moderate savers, to try and accumulate this kind of a down payment and closing costs.

Again, State actions can perhaps help this, but the real need is for something like the use of the IRA or Federal closing cost loan program.

The city of Baltimore has done a model pilot closing cost loan program. You get into a problem when you get into mortgages that are going to be brought in the secondary market, because many of those don't allow a second lien for a closing cost loan.

So it will take both Federal policy as well as Federal dollars, to provide some sort of a closing cost loan program that is viable.

Senator Cranston. John, do you have any questions?

Senator Chafee. I do, Mr. Chairman. Thank you.

Mrs. Cade, do you think it would help to keep housing costs down if we allowed commercial banks to underwrite municipal revenue bonds or mortgage-backed securities?

Are you at all familiar with that?

Mrs. CADE. I haven't put enough time and effort into that issue to give you a really good answer.

Senator CHAFEE. Anybody have any thoughts on that?

Let me ask, Mrs. Cade, I was jolted by your testimony, on page 9, where you stated that a $100,000 house would have total closing costs of $17,200.

That seems to me very, very steep. Now are you including in that prepayment of a year's taxes, recordation of tax transfer, tax conventional fees and the 10-percent down payment.

So, taking out the 10-percent down payment, which is $10,000, you have $7,000 for closing costs?

Mrs. CADE. Yes. Maryland's closing costs are extraordinarily high, particularly because of local recordation tax and local transfer tax. The State has a modest ½ percent transfer tax. And then, because we pay taxes at the beginning of the year, most lenders require that you ask for a 12-month—or a 14-month, in many cases, worth of taxes be put in escrow at closing.

And so those, cumulatively, along with title insurance and lawyers fees and all that, total over $17,000.

And I just yesterday testified at the State level on some steps that might be looked at for lowering closing costs in our State.

Senator CHAFEE. Well, I would hope the States would do that because this is a partnership. Obviously, the Federal Government can't carry the whole burden here. I would think, in relatively modest-priced houses, that the transfer tax might have an exemption of some type in there.

I was looking Mr. Dubno, at your chart on table B and the cost. And it leaps out at you that the land is the big feature.

Mr. DUBNO. Yes, sir.

Senator CHAFEE. I note the 63-percent increase in your period that you have there.

Let me ask you this. Yours is a wealthy State. You have towns that obviously set their own zoning. Is there any consideration being given in your State to requiring the various towns to accept some portion of low or median income housing at less than the three-acre or four-acre zoning, or whatever you have?

Mr. DUBNO. Yes, sir, there is. As a matter of fact, in this current legislative session they just passed a month ago, there were several bills that were proposed in order to literally force towns to do that.

I think the Governor and some of the other legislators feel that they want to develop some other kind of an approach, perhaps the carrot approach rather than a stick approach.

Senator CHAFEE. Well, the carrot's there. And your State obviously is giving plenty of State aid to every community.

Mr. DUBNO. Yes. Obviously, we're trying to address that problem and we're very much aware of it.

There are cities that are responding to this problem and are voluntarily making changes in their own local zoning laws. But I would agree with you that's a very big problem and it's not going to be resolved very easily in Connecticut.

Senator CHAFEE. I think there are a whole series of sociological factors that are assisted by spreading out the low income people in different communities so that they get the benefit of the better education and all that goes with it.

Let me ask you this, Mr. Hendrickson. Suppose you were king? What would you do to solve this problem? You could wave a wand and impose zoning as you wished. What would you do?

Mr. **HENDRICKSON**. Well, I would start at the local government level. And I think that it is clear that, at the local government level, they must in their land use planning take into account the need for affordable housing.

And I think one of the things that Florida did with a very comprehensive Growth Management Act in 1985 was to require local governments as part of their comprehensive plan to take into account the need for affordable housing and have that as part of their plan.

That's the first thing. The local government has to accommodate affordable housing, and they can't be an impediment to the production.

Senator **CHAFEE**. Do you mean Gulf Stream, FL, has some low-income housing?

Mr. **HENDRICKSON**. I don't know about Gulf Stream, but . . . clearly, in communities——

Senator **CHAFEE**. No, seriously, are they required to under this plan?

Mr. **HENDRICKSON**. They're not required to. What communities are required to do, all communities, is to develop comprehensive plan for development within the community, starting from now into the future.

And as part of that plan, affordable housing must be taken into account and the provision of affordable housing has to be part of their comprehensive plan that they're producing. And that is taking place.

Senator **CHAFEE**. There's a certain percentage of the community, *x*-percent of the land area?

Mr. **HENDRICKSON**. I can't give you the exact percentage.

Senator **CHAFEE**. No, but I mean is that the thrust of it?

Mr. **HENDRICKSON**. The thrust is that, within the development plan, it must have affordable housing as . . .

Senator **CHAFEE**. If people want to live in Greenwich, CT, they're entitled to live in a place that has five-acre zoning. But a certain part of that town would have to have some high density?

Mr. **HENDRICKSON**. It doesn't . . . again, I guess you can't undo what has been built in the past. That's not the purpose. But, where there is land left to develop and there is a comprehensive plan governing that development, affordable housing has to be part of that plan.

Senator **CHAFEE**. I see.

Mr. **HENDRICKSON**. I don't think that means that the city of Boca Raton, which, if it's fully developed within the city limits, is going to be retroactively required to, to change the use of land that's already been built out.

Senator **CHAFEE**. OK. Thank you, Mr. Chairman.

Senator **CRANSTON**. Thank you very much.

Bob, any questions?

Senator **GRAHAM**. I'd like to pursue a question that Senator Chafee asked. Another dimension of this committee, we're considering restructuring of financial institutions. One of the most contentious questions has been:

Should there be an expansion of the authority of commercial banks to engage in the underwriting of revenue-backed securities?

Currently, they are authorized to do so for general obligation, but not revenue-backed securities.

I would imagine that your State's housing represents a significant portion of the State issues and local issues of revenue-backed securities.

Had you found, in addition to difficulties, adequately competitive marketplace for underwriting of those securities?

Mr. DUBNO. I think there's an adequate market underwriting the securities. I also think that perhaps, if some of the commercial banks, given permission to participate in this process, they may make that market a little bit more competitive.

Senator GRAHAM. Mark, in your comments about the answer when you were attending to your world, the first thing that you would like to do is, at the local level, encourage planning which would provide facilities for a range of housing.

Are there any steps, either incentives, directives or others, that the Federal Government might take that would encourage local communities to give attention to the issue of affordable housing?

Mr. HENDRICKSON. Well, I think that's a question I'd want to give a lot of thought to to give you a comprehensive answer, but I think that if you come up with a housing bill for next year, that included some incentives for the down payment assistance, or other things, that you might very well want to tie the availability of that to some type of a local effort.

I know that, in the Affordable Housing Act that we passed in Florida last year, where there's a demonstration program using some State moneys to assist development, part of that is an absolute requirement that local government do something to lower the cost of housing being produced as a prerequisite of the State money going to a development in that community.

And I think that some parallel with the Federal program would be appropriate.

Senator GRAHAM. We focused on the financing of housing and its role in making housing more affordable. That's not an oxymoron.

In the context of the construction costs of housing, are there any recommendations in terms of Federal initiatives that might contribute from that side of affordability?

Mr. DUVERNAY. I would think that one of the good things that HUD had done in recent years is to look at the question of affordability both at the local level, in terms of codes and regulations, and at questions of construction costs and the like.

One of the things we're doing in Michigan in order to attempt to find new ways to address the construction cost is to, in the context of a technical staff of people—we have architects and engineers—to look at how we can either look at our regulations and deregulate them, or find a way to make cost construction savings.

One of the initiatives that my board took was to fund a competition, a cost competition, to find new ideas at making housing affordable. And we will award up to $20,000 for the best idea nationally.

And if there is also a State idea that's good, but not a national award, that, you know, we would award a $5,000 award.

And what we're doing is trying to stimulate ideas, either among students in architectural and engineering schools, or professionals who are now constructing housing and the like, and find some way to address the problem of not only the question of land or the question of interest rates, but how can we find a way to make the construction of homes affordable, or more affordable.

Mrs. CADE. We also are looking at working with people like the Enterprise Foundation. And they, through their research and we through some financing, can construct some houses that are perhaps lower in cost because of construction techniques or the simplicity of the housing itself.

We also have done housing energy-efficient designs that we make available for anybody throughout the State. And we also are proud that the National Association of Homebuilders Research Park on Housing Building Techniques is in Maryland. And we are looking to see what happens there, as all of us look at whether the specifications for construction should be changed, and how they can be made more cost-effective without loss of safety and efficiency in the house.

Senator CRANSTON. Jim Sasser, do you have any questions?

Senator SASSER. Mr. Chairman, I don't have any questions of this panel. I do have a statement which I would like to have included in the record.

Senator CRANSTON. Yes, it will be. Thank you.

I thank each of you very, very much.

We'll now go to our third panel.

I welcome each of you. Panel 3 will give us the industry perspective of this problem. The first witness is James Fischer, president of the National Association of Home Builders, Washington, DC.

I want to remind each of you, please, of the 5-minute rule. There's a green light up here while you have your 5 minutes; it becomes red when the 5 minutes are up.

We have 3 hours for this hearing and we're pretty much on schedule with the first two panels. We do have to close by about 12:25. So I urge you to stick to the 5-minute rule.

And, Mr. Fischer, we're now delighted to hear from you.

Senator SASSER. Mr. Chairman, if you would defer just a moment.

Senator CRANSTON. Certainly.

Senator SASSER. I would like to welcome once again before the committee this morning Mr. Jim Fischer, the 1987 president of the National Association of Home Builders.

Mr. Fischer is a resident of my hometown of Nashville. He's been in the building business for over 25 years. And during that period of time, he's built over 500 single-family homes and eight apartment complexes.

He was vice-chairman of the Tennessee Housing Development Agency for 6½ years, and is presently serving a 4-year term on the Metropolitan Nashville Planning Commission.

And I wanted to personally welcome Jim Fischer, who is a very distinguished citizen of our State of Tennessee, and a very successful businessman. And I'm proud to say, Mr. Chairman, a good friend of the Senator from Tennessee.

Thank you.

Senator CRANSTON. Thank you very much, and we welcome you again.

STATEMENT OF JAMES FISCHER, PRESIDENT, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. FISCHER. Thank you, Senator. Thank you, Senator Sasser. It's always a pleasure to be in front of my hometown Senator.

Mr. Chairman, my name is James Fischer and I am a home builder from Nashville, TN. I am testifying today on behalf of the 149,000 members of the National Association of Home Builders.

NAHB is a trade association of the Nation's home building industry, of which I am president. It is indeed a pleasure to appear before your subcommittee and not have to discuss FHA high-cost area adjustments or mobile home energy standards, or the other provisions of importance to us in this year's housing bill.

Senator CRANSTON. It's a relief for us, too. [Laughter.]

Mr. FISCHER. We can throw up some flags for that.

I commend you for giving us a unique opportunity in this series of hearings to explore key things in developing a renewed national housing policy. Perhaps no issue is more important than promoting the opportunity for homeownership, particularly for young families seeking to purchase their first home.

Earlier this year, we commissioned a national poll on the importance of housing to the American people. Mr. Chairman, the poll results were released to us in the last 24 hours. The poll was conducted by Dr. James Kitchen of Information America. The results, Mr. Chairman, show very strong for housing among the voters of this country.

Almost 80 percent of the voters agreed the Federal Government should take an active role in assisting homeownership.

Fifty-eight percent believe that housing has taken too large a share of Federal budget deficit cuts in recent years.

Two-thirds of the voters support the housing bill and urge Congress to override a veto if the President decides to veto this legislation.

Only 26 percent supported a veto of the housing bill in order to further reduce the Federal deficit.

Mr. Chairman, these are very significant and timely findings. We would hope that you would urge the administration to recognize the importance of this voter survey and continue to work to maintain housing as a high domestic priority.

Let me discuss the issues of homeownership affordability. I would like to quote from a publication of the U.S. Department of Commerce entitled "How To Own Your Home."

> Maintaining a high percentage of individual homeowners is one of the searching tests that now challenges the people of the United States. The present large proportion of families that own their own homes is both the foundation of a sound economic and social system and a guarantee that our society will continue to develop nationally as changing conditions demand.

The author, Mr. Chairman, was Herbert Hoover. The year was 1923. We met that challenge since World War II by changing from a Nation of renters to a Nation of homeowners. Fifty-six percent rented their homes in 1940, while 64 percent owned their homes in 1980.

Housing is of economic, social, and political importance to this country.

My written testimony graphically presents the numbers and the facts to support this.

Mr. Grider, author of now famous Atlantic Magazine article on David Stockman, and former national editor of Rolling Stone magazine, discussed one of the greatest reforms of the New Deal as, I quote:

> The Federal programs that permitted millions to buy homes which, under the old value system, they couldn't afford, for most Americans owning a home is their only real shot at accumulating wealth. I would say: If you are uncomfortable with the reality of how wealth is distributed in the United States, if you sincerely want to help ordinary families get their hands on real assets, then take the home builders campaign money and vote for housing with a clean conscience. Housing remains the best way yet devised to distribute wealth more broadly in our society.

In addition, homeowners are 50–75 percent more likely to vote than renters, according to the Census data. For the first time in 40 years, the homeownership rate in the United States is declining. This trend, which started in 1980, is most pronounced among young Americans looking to buy their first home.

Among married couples aged 25–29, homeownership fell from the rate of 59 percent in 1978 to 52 percent in the first quarter of 1987. This means 1.6 million fewer homeowners than would have been the case had the homeownership rate remained at its 1980 level.

The evidence is clear that it is tougher to buy a starter home today than it was a decade ago. The fundamental problem is that housing costs have risen faster than family incomes.

My written testimony tells the story in numbers. There are two trends which I believe are significant when you consider legislation in this area.

First, there has been a significant shift in the income prospects of many young families. The late baby boomers are finding their incomes and job opportunities squeezed by an enormous number of early baby-boomers who still have entry level jobs.

As these people grow older, the homeownership rate among middle-aged families—traditionally, the most stable—may well drop. Such a result could have a real impact on the politics of homeownership affordability.

Second, the problem of low-income homeownership opportunity, which is discussed in my written statement.

Mr. Chairman, my testimony details a number of key principles for a National Home Ownership Policy, which we have discussed with our friends, the realtors and the mortgage bankers as part of the joint policy statement we issued earlier this year.

I urge you to review these elements of a renewed housing policy. We view these hearings as a necessity first in step in exploring the problem of homeownership affordability.

I had the opportunity Monday to join Senator D'Amato and go through a Nehemiah Project in Brooklyn. And I would say that I was very impressed with it. We're going to have to continue the tax exempt financing as well as the Federal UDAG and Community

Development Block Grant Funds and State and local participation in order to achieve this all over the country.

I found that it was very necessary to helping the low-income people.

I thank you and the members of this committee for your interest in this important issue. I will be glad to answer any questions.

Thank you, sir.

[The complete prepared statement of James M. Fischer, Jr. follows:]

THE REPORT CONCLUDED THAT THE FHFA SHOULD ENCOURAGE LOCAL INDUSTRIES TO BUILD "DORMITORY STYLE" HOUSING FOR SERVICE WORKERS. CLEARLY, ALTERNATIVES AND INCENTIVES MUST BE FOUND AT THE LOCAL, STATE AND FEDERAL LEVEL BEFORE "DORMITORY STYLE" COMPANY OWNED HOUSING BECOMES THE BEST ALTERNATIVE FOR YOUNG FAMILIES.

ROLE OF THE STATE IN FLORIDA

IN FLORIDA, THE DEPARTMENT OF COMMUNITY AFFAIRS AND THE FHFA HAVE PRIMARY RESPONSIBILITY FOR HOUSING POLICY AND PRODUCTION. FLORIDA IS COMMITTED TO FINDING COST EFFECTIVE METHODS OF ADDRESSING THE HOUSING PROBLEM WITHOUT REPEATING THE EXTREMELY EXPENSIVE DEEP SUBSIDY PROGRAMS THAT THE FEDERAL GOVERNMENT HAS ABANDONED. FLORIDA'S HOUSING POLICY IS CENTERED ON A PUBLIC-PRIVATE PARTNERSHIP.

THE FHFA HAS BEEN FLORIDA'S MAJOR VEHICLE FOR THE PRODUCTION OF AFFORDABLE HOUSING IN THIS DECADE. OVER THE LAST SIX YEARS, THE AGENCY HAS SOLD OVER $2 BILLION IN BONDS TO FINANCE HOUSING FOR OVER 82,000 FLORIDIANS, WITH THE FIRST-TIME HOMEBUYER PROGRAM ACCOUNTING FOR OVER $1 BILLION OF THE FINANCING COMPLETED. THE PROGRAM HAS BEEN PARTICULARLY SUCCESSFUL IN URBAN AREAS OF FLORIDA, WHERE NEW JOB CREATION HAS CAUSED MASSIVE POPULATION EXPANSION. THE PROCEEDS HAVE BEEN EFFECTIVELY TARGETED TO LOW AND MODERATE INCOME FAMILIES, WITH THE AVERAGE

HOUSEHOLD INCOME OF PERSONS SERVED BY THE PROGRAM CONSISTENTLY BETWEEN 95%-100% OF STATE MEDIAN INCOME.

DUE TO THE PROBLEMS PREVIOUSLY ADDRESSED, THE HOMEOWNERSHIP PROGRAM HAS BEEN MORE DIFFICULT TO IMPLEMENT OVER THE PAST TWO YEARS. HOWEVER, WITHOUT TAX-EXEMPT BOND FINANCING, THE PROBLEM OF AFFORDABILITY FOR YOUNG FAMILIES WOULD BE MUCH GREATER. THE SUNSET OF FIRST-TIME HOMEBUYER BONDS AFTER 1988 MUST BE AVOIDED.

FLORIDA'S COMMITMENT TO ADDRESSING THIS PROBLEM IN A PARTNERSHIP WITH THE PRIVATE SECTOR AND THE FEDERAL GOVERNMENT GOES BEYOND RHETORIC. FLORIDA HAS CREATED A DEMONSTRATION LOAN PROGRAM WHEREIN LOW INCOME HOMEBUYERS CAN RECEIVE A STATE FUNDED 0% LOAN ON ONE-THIRD OF THEIR MORTGAGE. THIS, AND OTHER DEMONSTRATION LOAN PROGRAMS ARE TO BE REVIEWED BY THE GOVERNOR AND LEGISLATURE FOR POSSIBLE EXPANSION IN 1988.

CONCLUSION

THE MODERATE INCOME FIRST-TIME HOMEBUYER FACES PROBLEMS TODAY THAT DID NOT EXIST A DECADE AGO. HOUSING COSTS ARE RISING FASTER THAN FAMILY INCOME, CREDIT UNDERWRITING STANDARDS ARE STRICTER, MORE CASH IS NEEDED TO CLOSE A LOAN, AND INCREASED RENTS MAKE IT MORE DIFFICULT TO ESTABLISH THE CREDIT HISTORY AND SAVINGS ACCOUNT NECESSARY FOR HOMEOWNERSHIP. THE PROBLEM IMPACTS A WIDE RANGE OF FAMILIES, NOT JUST THE POOR. PROGRAMS SUCH AS

TAX-EXEMPT BOND FINANCING, FHA MORTGAGE INSURANCE, AND CONTINUED FEDERAL INCENTIVES TO THE SECONDARY MARKET ARE ESSENTIAL TO FAMILIES BUYING THEIR FIRST HOME. AFFORDABLE HOUSING IS NOT A LUXURY, IT IS ESSENTIAL TO THE HEALTH OF AN EXPANDING ECONOMY. THE SOLUTION WILL REQUIRE A FEDERAL, STATE AND PRIVATE SECTOR PARTNERSHIP TO REMOVE DISINCENTIVES AND CREATE INCENTIVES FOR THE PRIVATE SECTOR TO DEVELOP AFFORDABLE HOUSING.

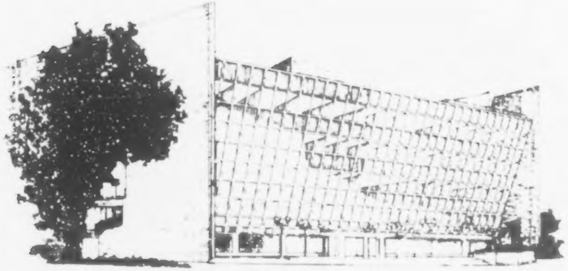
Statement of the NATIONAL ASSOCIATION OF HOME BUILDERS before the

Committee Senate Committee on Banking, Housing and Urban Affairs
Subcommittee on Housing & Urban Affairs

Subject Declining Affordability of Homeownership

Witness James M. Fischer, Jr.

Date July 1, 1987
Place Room 538, Dirksen Senate Office Building



National Housing Center
15th and M Streets, N.W.
Washington, D.C. 20005
(202) 822-0470

Mr. Chairman, my name is James M. Fischer, and I am a homebuilder from Nashville, Tennessee. I am testifying today on behalf of the 147,000 members of the National Association of Home Builders (NAHB). NAHB is a trade association of the nation's home building industry of which I am President. It is indeed a pleasure to appear before your Subcommittee and not have to discuss FHA high-cost area designations or mobile home energy standards -- or the other provisions of importance to us in this year's housing bill. I commend you for giving us a unique opportunity in this series of hearings to explore key themes in developing a renewed national housing policy.

Perhaps no issue is more important than promoting the opportunity for homeownership, particularly for young families seeking to purchase their first homes. Mr. Chairman, may I quote from a publication of the U.S. Department of Commerce entitled "How to Own Your Home" --

> Maintaining a high percentage of individual homeowners is one of the searching tests that now challenge the people of the United States. The present large proportion of families that own their own homes is both the foundation of a sound economic and social system and a guarantee that our society will continue to develop nationally as changing conditions demand.

The author, Mr. Chairman, was Herbert Hoover. The year was 1923.

And we met that challenge since World War II, by changing the complexion of our country from a nation of renters (56.4 percent rented) in 1940 to a nation of homeowners (64.4 percent owned) in 1980.

As you know, homeownership provides benefits to society far beyond the provision of decent shelter. These effects are economic, social, and political. Obviously, housing construction has a substantial direct impact in terms of job creation for construction workers, building material suppliers, and the entire network of subcontractors. In addition, there is a significant multiplier effect on the broad range of industries which provide products for the home, including furniture and appliance manufacturers, retailers and the like. The construction of 100,000 single family homes generates:

- o 176,000 worker-years of employment in construction and related industries
- o $4.15 billion in wages
- o $1.25 billion in federal, state and local tax revenues.

Housing is important to the health of the economy. It leads the economy out of recessions. For example, while investment in housing accounted for only 4.5 percent of our real gross national product in 1983, it was responsible for about 39 percent of the *total* economic growth during the first full year of recovery. In 1986, real GNP grew at a 2.5 percent rate, while residential fixed investment grew by 9.6 percent -- almost four times as fast.

The social benefits of housing are perhaps less tangible, but probably equally as important. Homeownership promotes

privacy and a sense of pride that accompanies ownership and the upkeep of property. It helps contribute to the stability and well-being of the American family. Homeownership has often been referred to as the American Dream, a goal that motivates millions of our citizens to work hard, get a good education and a good job so that one day they will be able to own a home of their own.

A related point was eloquently made by William Greider, author of the now-famous Atlantic magazine article on David Stockman and former national editor of Rolling Stone magazine. He discussed one of the great reforms of the New Deal -- "the federal programs that permitted millions to buy homes which, under the old value system, they couldn't afford" in a speech before House Democrats at the Greenbrier in March 1985. He said, "For most Americans, owning a home is their only real shot at accumulating wealth . . . I would say -- if you are uncomfortable with the reality of how wealth is distributed in America, if you sincerely want to help ordinary families get their hands on real assets, then take the Homebuilders' campaign money and vote for housing with a clean conscience. *Housing remains the best way yet devised to distribute wealth more broadly in our society*." (Emphasis added)

Finally, it may be said that the most important aspect of promoting homeownership opportunity is political, as Herbert Hoover recognized in 1923. Owning your own home gives people the opportunity to become a part of our capitalist system. This process promotes the development of a middle class, which has historically reflected political stability and security. For example, homeowners are 50 to 75 percent more likely to vote than renters, according to Census data. And they have a stake in the stability and prosperity of their community and the country.

A major national survey of homeownership attitudes completed in 1982 found that the goal of homeownership is desired by virtually all people -- more than 75 percent said that owning a home is extremely or very important to them personally. However, one-third of those interviewed agreed with the statement, "I'll never be able to own the kind of home I want," and 80 percent said that in the future, fewer people will be able to afford a home. (We must acknowledge that this survey was conducted in 1982 when interest rates were at a peak).

The values of homeownership, as described by the people surveyed, should not surprise you. Over 80% agreed that homeowners have more privacy than renters, live in better maintained neighborhoods, and that homeownership provides a sense of involvement in the community. And over 70 percent believe that a home provides a better environment to raise children. In short, homeownership represents a better quality of life.

Most Americans (88 percent) still believe that owning a home is a good investment -- a hedge against inflation and a good way to save for retirement. Most importantly, 86 percent agreed that homeownership should be made available to every American who wants to own a home.

The government role in promoting homeownership has widespread public support. Seventy-five percent said that the federal government should at least maintain its current programs (like FHA and VA) or do even more to help people buy homes. Over 40 percent said that the government should do everything possible -- more than it is doing now -- to promote homeownership. The public's view is somewhat different than that of Congressional tax writers and the Office of Management and Budget. Forty percent believe that the government should find ways to help people who want to buy homes -- even if there were fewer tax incentives.

Finally, the survey analyzed the political impact of the homeownership issue. A candidate who says, "More should be done to help young people who can't afford to buy a home" is favored 73 percent to 13 percent by the public. And one who says, "High interest rates are destroying a basic right of Americans to buy or sell homes when they want or need to" gets a positive rating of 70 to 17. I believe that Presidential candidates are just beginning to understand the potential benefits of advocating policies which promote housing opportunity. So much for the public attitude toward homeownership.

An historical perspective will help us understand the nature of the homeownership affordability problems we face today.

HOMEOWNERSHIP IN RETROSPECT

Much of the shift toward homeownership occurred in the late 1940's and 1950's.

- Family income grew considerably.
- Young people were getting married at an early age, and having more children.
- Interest rates were low.
- Home prices rose, but not much faster than the inflation rate.

But we must emphasize the importance of conscious and vigorous federal policies which expanded homeownership opportunities during this time.

- Long-term, low-downpayment mortgage loans insured by FHA.
- No downpayment loans guaranteed by VA for returning veterans and their families.
- The promotion of a strong savings and loan industry dedicated to providing adequate and affordable residential mortgage loans.
- A well-funded federal highway and infrastructure program which promoted mobility and opened up suburban development.

The rate of increase in homeownership slowed during the 1960's, partly due to an increase in interest rates from 5.9 percent in 1965 to 8.2 percent in 1970. The shift toward later marriages, more divorces and more single-person households also had an effect on overall ownership, but not, of course, on the ownership opportunities of individuals.

The trends against homeownership were even greater in the 1970's, with more younger households and more single people entering the market. But these were largely offset by the phenomenon of "inflationary expectations" which was caused by rapid appreciation in home values. This was aided by a growing and effective secondary mortgage market to purchase FHA, VA and conventional mortgages at Ginnie Mae, Fannie Mae and Freddie Mac. The train was leaving the station, and everyone who could afford a ticket wanted to be on it. Mr. Chairman, the "trains" were particularly crowded in California, and there were frequently lotteries and long lines to buy scarce homes which came on the market. Low effective "real" interest rates (net of expected inflation) made the effective cost of homeownership low compared to renting. This pushed homeownership rates to new highs -- as high as 59 percent for young married couples in 1978.

Those families who were able to purchase homes in the 1970's, as with those of our generation who bought our first homes with FHA or VA mortgages after World War II, are reaping the benefits of homeownership and building equity today.

But the problem of declining affordability faces those young people coming of age in the 1980's -- our sons and daughters, and the younger brothers and sisters homebuying generation of the 1970's.

DECLINING HOMEOWNERSHIP TRENDS IN THE 80'S

For the first time in 40 years, the homeownership rate in the U.S. is declining. This trend, which started in 1980, is most pronounced among young Americans considering purchasing their first home. How serious is the situation? The homeownership rate among all households peaked in 1980 at 65.6 percent. Since then, it has fallen to 63.8 percent. Among married couple households in the 25 to 29 age group, homeownership fell from a rate of 59 percent in 1978 to 52 percent in the first quarter of 1987. For married couples in the 30-34 age group, the homeownership rate fell from 75 percent in 1978 to 70 percent in 1985. Part of the decline in the overall ownership rate will undoubtedly be made up in the years ahead as the general population ages. But it still represents a significant drop in housing opportunities. This translates into 1.6 million fewer homeowners than would have been the case had the homeownership rate remained constant at its 1980 level. Moreover, the homeownership rate of this younger generation is likely to continue to lag behind the preceding generation.

The concerns of young families priced out of the homeownership market quickly spread to other age groups, particularly the 34 million parents with children under 18 who are wondering whether their children will ever be able to buy their own homes.

To some degree these shifts in homeownership have been heightened by rising expectations, demographics and the record high interest rates suffered in the early 1980s. Housing standards of most Americans have increased over the past 40 years, despite intermittent setbacks suffered during recessions and hard economic times. But expectations have also risen. Americans today want better built and equipped starter homes than their counterparts of twenty or even ten years ago. Air conditioning, energy saving features and modern appliances -- once considered luxuries or not even envisioned -- are now viewed as standard equipment.

Demographic trends have also had disruptive impacts on homeownership opportunities. In the 1970s a record number of Americans born following World War II began flooding the housing and job markets, creating a situation where there were upward pressures on the price of homes and downward pressures on wage rates. Many in the first wave of the 1970s were lucky enough to purchase their first home before inflationary pressures in the mid 1970s sent housing prices soaring. They also beat the spike in interest rates that hit the market in the early 1980s. But those who followed in their footsteps got hit by a triple whammy -- higher prices, higher interest rates and lower incomes. Consequently, many of them discovered that the costs of buying a home had been pushed beyond their reach.

But even taking into account today's high expectations among young Americans and the nuances in the numbers caused by demographic factors and unusual economic conditions, the evidence is clear that it is tougher to buy a starter home today than it was a decade ago. The fundamental problem is that housing costs have risen faster than family incomes.

Some basic math illustrates the problem. In 1975, median family income was $13,719 and the basic new single-family home cost $42,700, requiring an annual income of $15,775 to qualify for a 90 percent loan at 9 percent interest. In 1985, while median incomes had doubled to $27,735, the same house cost $92,200, an increase of 116 percent. Even more striking, at today's 10 percent interest rates, an income of $37,657 would have been required to purchase that home, up 132 percent from the income required to buy the same home in 1975. Ups and downs in interest rates, of course, change the affordability equation. When mortgage rates reached a peak of 17 percent in 1981 and 1982, the number of Americans qualifying for loans fell dramatically and the housing market was virtually shut down.

Because the affordability equation changes with swings in interest rates and local economic conditions, many households have accepted some trade-offs to make the numbers work for them. They have, among other things, borrowed from their parents, delayed having children, devoted a much larger portion of their take-home pay to cover housing expenses and increasingly relied on a second wage earner. Since 1970, the percentage of married

households with two wage earners has increased from 44 percent to 62 percent. But mostly they have put off home purchase, waiting to increase their savings and their incomes.

Buying a first home has always been difficult for most families. It requires thrift, patience and sacrifice -- virtues that are worth cultivating. But the issue today is how much more can young households be expected to give up to join the ranks of homeownership. There is a limit to how far households can stretch their budgets to purchase a home. Furthermore, those limits are being reduced by lenders and mortgage underwriters who have tightened qualifying loan standards because of concerns regarding mortgage defaults.

Why should existing owners care about declining opportunities for first-time buyers? In many cases it involves the future of their own children. Secondly, existing home owners have a vested financial interest in keeping the door open. First-time buyers are essential to the entire housing chain. Without a steady flow of new customers entering the market, existing owners will have trouble selling their homes and trading up to better quality and larger homes in more desirable neighborhoods.

In addition, continued slippage in homeownership affordability could have far reaching implications for American lifestyles and living patterns in general. Decisions to marry or have children could be postponed. Job opportunities could be rejected, particularly when they involve moving from an inexpensive market to a high-cost one. Ultimately, the cost of housing influences where we live and how we live.

There are two final trends which I believe are significant when you consider legislation in this area.

Along with current affordability problems for young families, there has been a significant shift in the income prospects of many younger households. During the 1981-82 recession, much of the increase in unemployment was among younger households. The late baby boomers, currently in the homebuying age of 25 to 29 are finding their income levels and promotion prospects squeezed by the enormous number of employees preceding them into entry-level jobs.

The large numbers of Americans born at the peak of the postwar baby boom in the late 1950s have not done as well economically as earlier generations. To a large extent, this is because their greater numbers have swamped the labor market, and real wages for the group have been forced down. Despite the large numbers of two-earner households among this group, the average incomes of late baby boomers have been low relative to other groups. In 1965, the average income of families 25 to 30 years old was equal to 96 percent of the average income among families. By 1975, as the first wave of the baby boom entered the 25 to 34 year old bracket, that ratio fell to 92 percent. In 1985, the incomes of households headed by people 25 to 34 years old averaged only 81 percent of the average income for all families.

Interestingly, as this population ages, the homeownership rate among middle-age families -- traditionally the most stable -- may well drop. Currently, middle-income families in the 45 to 64 age group have a homeownership rate of 88 percent. We fear that this rate will decline over time because younger households will not "catch up" in homeownership patterns unless affordability improves. Such a result could have a real impact on the "politics" of homeownership affordability.

Finally, the dual problems of low-income homeownership opportunity. Homeownership has always been difficult to achieve for lower income households. Currently, ownership among those with incomes under $15,000 is half of what it is for those making $50,000 or more. Some of this differential is due only to differing age and household status. But even among married couples aged 25 to 29, the difference in homeownership rate at the top of the income ladder and the bottom is 40 percentage points.

Overall, this income-related differential has expanded in recent years. Lower income households are more vulnerable to all of the negative forces affecting affordability. They have to rely on low-downpayment loans, they more often barely qualify for financing, and they are more likely to be priced out of the market by local fees and restrictions.

Yet lower-income families share the goal of homeownership. For this segment of society, I sense a growing mood of helplessness and hopelessness. That is the psychiatric definition of clinical depression in an individual. I am not certain we know how to deal with "depression" in large segments of the lower class of society.

CONCLUSION

Mr. Chairman, we have just begun to focus on specific recommendations for federal action. They arise out of a report drafted by NAHB in January, "A Blueprint For National Housing Policy," and a joint policy statement agreed to by my fellow panel members, the National Association of Realtors and the Mortgage Bankers Association.

Several observations are evident from our analysis. Current and ongoing efforts to promote homeownership opportunity remain essential. In addition, there are a number of new areas to explore to reduce housing costs.

- The continuation and promotion of federal insurance and guarantee programs that enhance the availability and reduce the cost of housing at little or no cost to the federal government is essential.
- The continuation and promotion of federally related programs and institutions that provide access to credit through well-developed secondary markets, including Ginnie Mae, Fannie Mae and Freddie Mac is essential.
- Maintenance of a commitment to housing finance through a viable system of thrift institutions backed by a strong Federal Home Loan Bank Board system and a revitalized Federal Savings and Loan Insurance Corporation remains essential.

- Tax incentives for homeownership, including the mortgage interest and property tax deductions and mortgage revenue bonds, are an integral part of a national housing policy.
- Regulatory barriers and a variety of fees that unnecessarily reduce the affordability and constrain the supply of housing should be reduced and eliminated.
- The cost of constructing and maintaining community infrastructure should be fairly apportioned among all those who use or benefit from these facilities -- not imposed solely on the new homeowner.
- Government policy should encourage development and implementation of cost-saving technological advances as well as the availability of an adequate supply of skilled labor for home building.
- Acknowledgement of the increasing capacities of state and local governments, particularly through the innovations of state housing finance agency programs and the development of creative public/private partnerships, in future federal housing legislation.

There are a variety of other options to explore to promote widespread homeownership opportunity.

- On Monday, I joined Senator D'Amato for a tour of the Nehemiah project in Brooklyn, a program which is authorized for broader use in both the Senate and House provisions of the housing bill.
- We have long supported tax incentives to help first-time homebuyers meet downpayment requirements. First time homebuyers should be permitted to withdraw limited amounts from IRA or 401(k) tax-deferred savings accounts without penalty if used for downpayments on their homes.

Mr. Chairman, we view these hearings as the necessary first step in exploring the problem of homeownership affordability. I have attached to my statement an economic analysis of trends in homeownership prepared by NAHB's Economics, Mortgage Finance and Housing Policy Division for your review. We look forward to the opportunity to continue to work with you and your highly competent staff as you develop comprehensive legislation for the 1990's. We congratulate you on making this effort a high national priority and stand ready to offer our resources toward our mutual goal. I will be pleased to answer any questions you may have.

TRENDS IN HOMEOWNERSHIP:
PAST, PRESENT AND PROSPECTIVE

Prepared for Submission with the Testimony of
the National Association of Home Builders
to the
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Economics, Mortgage Finance, and Housing Policy Division
National Association of Home Builders

TRENDS IN HOMEOWNERSHIP:

PAST, PRESENT AND PROSPECTIVE

For the country as a whole, the homeownership rate reflects the summation of the decisions of individual Americans. For any individual household, becoming a homeowner depends mostly on income, age and family status. For example, over 90 percent of married households with heads over the age of 45 and with incomes over $30,000 are homeowners, but homeownership is less than 30 percent among married households under age 30 and with incomes less than $15,000. However, income and demographics are not the only determinants of homeownership. Achieving homeownership also requires affordability, including supportable mortgage payments, downpayments and other mortgage terms, and reasonable home prices. Other important elements in the affordability equation are tax savings and appreciation potential.

Thus, national trends in homeownership reflect the combined trends in demographics, the economy, mortgage markets, and the overall cost of owning versus renting. As shown in Figure 1, from 1940 to 1980, these trends were generally highly supportive of homeownership, changing the country from a nation of renters (56.4 percent rented) in 1940 to a nation of homeowners (64.4 percent owned) in 1980. The factors having the greatest influence on the ownership rate varied from decade to decade, but the supportive forces always outweighed the negative ones, until the 1980s. This decade is very likely to witness the first decline in homeowning since the decade of the Great Depression.

Homeownership: 1940-1980

Most of the shift to homeownership occurred during the late 1940s and the 1950s, when nearly everything was working towards expanding homeownership. Real median family income grew at a 3.2 percent annual rate from 1950 to 1960.

The age of marriage was declining and the number of children per household was expanding. Interest rates were low, both in absolute levels and relative to inflation. House prices rose rapidly after WW II, but appear not to have risen faster than inflation over the rest of the period. Simultaneously, long-term, low- or no-downpayment loans were readily available with FHA or VA backing and the savings and loan industry was a strong and efficient source of mortgage funds.

The rate of expansion in overall homeownership slowed markedly during the 1960s. Why? The answer is part demographics and part economics. While real income continued to grow rapidly, average mortgage rates rose from 5.9 percent in 1965 to 8.2 percent in 1970. Over the decade, the shift towards later marriages, more divorces and more single living accelerated. In fact, married couples as a share of all households fell from about 75 percent to 69 percent over the decade.

The demographic trends adverse to homeownership accelerated during the 1970s. The typical household was younger and more likely single, with the share consisting of married couples falling further to only 61 percent by 1980. Yet these demographic trends were offset by a new economic phenomenon--major inflation in house prices. Although mortgage interest rates trended upwards during most of the 1970s, expectations of appreciation soared faster as inflation psychology took hold. The net effect was an effective "real" (net of expected inflation) interest rate that was low, if not below zero, and an effective cost of owning that fell relative to rents. The outcome was a widespread shift towards ownership that pushed homeowning to new highs.

The Recent Decline in Homeowning

The decade of the 1980s has had the advantage of demographic pressures more favorable towards ownership than in the 1970s. The baby boomers have [illegible] but only the continuing decline in the share of married couples [illegible] been acting to hold down overall ownership rates. However, [illegible] economic trend has been against ownership since 1979. [illegible] interest rates were followed by high unemployment and slow income growth [illegible] continued high real house prices and sharply lower appreciation [illegible]. Then a steady rise in real rents has failed to [illegible] homeownership. The net effect has been a [illegible] decline in overall homeownership of [illegible] percent from the peak reached in 1980 (see Figure 2). This represents [illegible] million fewer homeowners than would have been the case if ownership had simply stayed flat.

In this review of the trends in homeownership [illegible], the overall homeownership rate [illegible] into a combination of purely demographic factors with economic and housing market factors. Since only the economic and housing market factors are subject to policy change, it is useful to isolate their impacts from the impact of demographics. This can be done by tracking the homeownership rate for a specific age and household type. Consider, for example, married couples between the ages of 25 and 29. This group includes a large proportion of first-time home buyers. Thus the pattern of homeownership for this group is most reflective of both the economic and policy-relevant factors.

The impact of the recent adverse economics is reflected clearly in the data available through the Annual Housing Survey from 1974 to 1980 and the Current Population Survey since 1980. The homeownership data for young married couples, presented in Figure 3, show a slight decline from 1978 to 1980, followed by a sharp fall-off between 1981 and 1982, as the full brunt of the high interest rates hit the housing market. Then, for a couple of years, homeownership stabilized for this group as interest rates fell and adjustable

rate mortgages (ARMs) brought more households into the home purchase market. However, homeownership rates have fallen steadily again for young married couples since 1984, right through to March of 1987. Current levels are significantly lower than those in 1974, before inflation-motivated buying set in. The recent rise in interest rates will only further delay a recovery in homeownership for this group.

Homeownership Affordability Today

Becoming a homeowner has always involved major cash outlays. Up-front costs include application fees, origination fees, legal fees, and points, all on top of the downpayment. For most younger families, the process consumes nearly all of their savings. In addition, at current interest rates and house prices, the monthly mortgage payment will divert a quarter or more of the household's income, at least until the household income rises substantially. Moreover, selling a house is much more complex and expensive than vacating a rental unit.

Because homeownership is a serious financial endeavor, it is not undertaken lightly. The fact that nearly all households that have the opportunity do become homeowners reflects the strength of the personal benefits from owning their own home, as well as long-term financial benefits. But the decline in homeownership since 1980 indicates an increased difficulty and financial unattractiveness of becoming a homeowner.

Mortgage Interest Rates

The first blow to housing affordability was the surge in mortgage interest rates starting in 1979 and peaking at levels which averaged over 15 percent in 1982. These rates posed a crushing burden on the budgets of many homebuyers, and, not surprisingly, disqualified them for financing. However, the impact was softened by extensive efforts to revise underwriting criteria and to create arrangements such as buydowns and graduated payment mortgages (GPMs), which allowed households to qualify under existing criteria. At the time, these were viewed as reasonable because of the rapid inflation in incomes and house prices experienced since 1975. Only later did "disinflation" set in suddenly, sharply reducing growth in incomes and house prices and, relatedly, deflating the economies of agricultural and natural resource regions.

In 1987, mortgage rates are back in the 10 percent range and, as long as they stay there, mortgage payments do not generally pose an unbearable burden on incomes, even for first-time buyers. However, as a reaction to problems with loans made in 1981-82, underwriting standards have been made as restrictive or more so than before then. These standards will quickly choke off access to fixed rate financing if mortgage rates move up significantly from current levels.

As noted, a number of new mortgage instruments and arrangements were created or expanded in the dark days of 1982. In addition to the buydowns and GPMs, tax-exempt mortgage revenue bonds (MRBs) played a key role in keeping the window of opportunity open, especially in 1982. Soon thereafter, a steep decline in short-term interest rates and the removal of regulatory restrictions allowed lenders to offer ARMs at affordable levels. So MRBs and ARMs let first-time homebuyers back into the market until long-term fixed-rates could drop to the 10-12 percent range.

With the steady decline in interest rates on fixed-rate mortgages throughout 1985 and 1986, there had been hope that homeownership would rebound, especially among younger households. This hope was premature. Homeownership among young households declined further. The single most important reason for this is probably the sharp decline in house price inflation relative

to mortgage interest rates. If one can handle the payment burden, a 12 percent interest rate does not look too bad if the house price is going up at 10 percent per year. But in 1986, the price of a given typical new home (i.e., holding its size and other characteristics constant) rose only 1.2 percent, while mortgage interest rates averaged about 10 percent, leaving a net real interest cost of about 9 percent. Even if buyers expect some resurgence of house price appreciation in the next few years, perhaps towards 5 percent, a real interest cost of 5 percent still would be high relative to historical standards. (Of course, the problem is not that inflation is too low, but that real interest rates are too high.)

House Prices

Compounding the impact of high real interest rates have been high real house prices. In most of the country, prices shot up faster than inflation and incomes during the 1970s. In the 1980s, house prices have slightly lagged inflation on average, although in some areas, especially the Northeast, there have been much larger increases. The continuation of prices at high levels has been good from the point of view of holding down defaults and maintaining confidence in housing as an investment. But the high prices are gradually translating into higher housing costs across the board, for renters and owners.

It was commonly held that the run-up in prices in the 1970s reflected the inflation psychology of the period and the high demand by the baby boomers. Thus, some are puzzled by the continuing high prices and even a new resurgence in the Northeast. But, it should not be surprising that these price increases are sticking because, over the last 10-20 years, layer after layer of regulations, restrictions and fees have been put on home building, mostly at the local level. Sometimes this causes a steady upward trend in prices, as, for example, when sidewalk and road-width requirements rise or sewer fees are added. Other times the results have been more spectacular, as when a surge in demand hits a development approval process so slow and expensive that buyers have to resort to open bidding against each other for the few homes available. The latter has happened in areas of both the Northeast and the West and left these areas facing local housing affordability crises.

Restrictions such as large lot zoning and high per-unit fees have not only raised the cost of houses generally, but have also directed development towards large, expensive housing for older, wealthier trade-up buyers and away from the construction of affordable housing for first-time buyers.

In areas where house prices have been steady or declining, the cash outlays required to achieve homeownership have not been pushed up, but the apparent affordability of housing in such areas has been offset by fears about the reasonableness of homeownership as an investment and about the credit risk of mortgage lending. Thus, many lenders have imposed especially stringent underwriting standards in such areas.

Downpayments

A key element of affordability is the downpayment requirement. During the 1970s, the downpayment burden was generally easing, as private mortgage insurers began offering a 5 percent downpayment option. Since 1982, however, low downpayment options have been eliminated or tied in to severe underwriting restrictions. This has renewed the first-time buyer's traditional reliance on FHA or VA financing.

Tax Savings

Even the long-standing assistance provided by the Tax Code has been reduced, first by the 1981 Tax Act and now by the 1986 Tax Act. The most direct impact of these tax changes has been reductions in tax brackets and thus in the value of homeowner deductions. The changes in tax rates have not been overly significant for affordability, but the scheduled increase in the standard deduction in 1988 will be. For example, since a married couple receives a $5,000 deduction without having any itemized expenses, and there will be few itemizible expenses other than homeowner deductions, the tax savings on getting even $7,000-$10,000 in homeowner deductions will be relatively small.

Income Trends

Coinciding with the current homeowner cost problems facing younger households has been a significant shift in the income prospects of many of these same households. During the recession of 1981-82, the great bulk of the rise in unemployment was among younger households. Moreover, the second half of the baby boom, currently centered in the homebuying ages of 25-29, are finding their income levels and promotion prospects squeezed by the enormous number of employees who preceded them into entry level jobs. Their real wages have been depressed by the increased competition for jobs, as well as other basic economic trends, such as deregulation, foreign competition and the continuing decline in union influence.

The result has been that those born at the peak of the postwar baby boom in the late 1950s have not done as well economically as earlier generations. Despite the large numbers of two-earner households among the baby boom cohort, the average incomes of late baby boomers have declined relative to other age groups. In 1965, the average income of families (this category excludes singles) headed by people 25 to 34 years old was equal to 96 percent of the average income among all families. By 1975, as the first wave of the baby boom entered the 25 to 34 year old bracket, that ratio fell to 92 percent. In 1985, the incomes of families headed by people 25 to 34 years old averaged only 91 percent of the average income for all families.

Low-Income Homeownership

Homeownership has always been difficult to achieve for lower-income households; currently ownership among those with incomes under $15,000 is half of what it is for those making $50,000 or more. Some of this differential is due only to the differing age and household status of low- and high-income households. But even among married couples aged 25-29, the difference in the homeownership rate at the top of the income ladder and the bottom is 40 percentage points. This is not surprising, given the high cash costs of ownership discussed above.

Overall, the income-related differential has expanded in recent years. Lower-income households are more vulnerable to all of the negative forces affecting affordability. They have to rely on low-downpayment loans, they more often barely qualify for financing, and they are more likely to be priced out of the market by local fees and restrictions.

Homeownership Prospects

The adjustment to an era of high real interest rates, high real house prices, and tightened underwriting standards may not be over yet. Even if none of these or other factors worsen in the future, homeownership among younger households may continue to decline, simply as a delayed reaction to past events. As long as this decline is not too sharp, though, overall homeownership rates may start to rise as the baby boomers age.

Most prospects for change are also not encouraging. The lag in relative income trends of the late baby boomers will probably continue as they age (although the baby bust generation will do relatively well). Real house prices are becoming subject to renewed upward pressures from additional federal regulation (e.g., on wetlands or water runoff), as well as rising anti-growth attitudes in many parts of the country. Most importantly, real interest rates will probably not decline in the near future and nominal interest rates could rise further if inflation shows signs of increasing.

The most positive force behind homeownership in the near term may be the upward pressures on rents which will eventually follow the enactment of the 1986 Tax Act. Higher rents may convince households to act on homeowning, but, of course, for the low- and moderate-income household without a viable ownership option, higher rents simply means a lower standard of living.

Senator CRANSTON. Thank you very much.

Now we go to Ira Gribin, first vice-president of the National Association of Realtors.

Ira, I welcome you. We collaborated for many, many years. And I thank you for coming all the way across the country.

STATEMENT OF IRA GRIBIN, FIRST VICE PRESIDENT, NATIONAL ASSOCIATION OF REALTORS

Mr. GRIBIN. Thank you, Senator Cranston. We certainly want to congratulate the committee for holding these hearings and, equally important, for the fact that the housing bill you've passed is the first freestanding bill in 6 years. And we pledge you, as the realtors, to do everything possible to get it passed. And mostly, if there is a veto, to do everything we can to help override the veto.

First of all, I want to say ditto to almost everything else everybody said because, basically, we're almost in complete agreement.

Five times in this century we have reaffirmed a commitment to decent and affordable housing, and a suitable housing for every American.

I see, and our organization sees, housing as a ladder. And it's not complete without that ladder and all the steps to it.

The first level of those ladders and the first few steps of those ladders are really rental housing for the very low, and the low and moderate income groups.

Before you own a home, you need to get into affordable housing, meaning rental housing. And your committee is to be commended for looking at all phases of it.

As you move up that ladder, you get to that first-time buyer and then, ultimately, to the second and third time buyers. Ultimately, we go up that ladder.

But there's simply no question in our minds that, in order to move up that ladder, you've got to start on that ladder, and that rental housing is a part of it. And we need a partnership between the public sector and the private sector.

We submitted an exhibit which indicates that in 1986, a Roper Survey shows that the top choice among 85 percent of the people in this country was that the things that make up a good life was owning a home.

I think there's no question about it, it's truly the American Dream. Having just returned from the Soviet Union, I am more convinced of that than ever before.

I think there are three factors that go into making up housing affordability. The first factor—it's like a three-legged chair, it won't stand with two legs. I'm sorry Senator Chafee left because I would like to have discussed this with him as one of the factors.

One is the price of the down payment. The other is the income to produce that down payment. The last thing is the financing of the rates. You need all three legs to make it stand.

Let me give you some examples. The median price for a home in 1970 in the United States was $23,000. In California, it was approximately $24,000. In 1986, it went up from $23,000 to over $80,000 in the United States. And in California, from approximately $24,000 to over $131,000. An increase of 249 percent in the United States and 441 percent in California.

As it relates to median income in 1970, the median income in the United States was almost $10,000. It's gone up almost to $28,000. That's an increase of 183 percent. And, in California, from $10,800 to $30,800, about the same increase but behind the increase in housing prices.

As it relates to financing, housing affordability if measured by a ratio of housing expenses to income in the United States was 20.3 percent in 1970; it's now 26.7 percent, almost a 30-percent increase. And in California, from 21 to 39 percent—almost a 200-percent increase.

These are the facts as we know them. We've gone from a 65.6-percent homeownership rate; in 1980 to 63.8 percent in 1986.

That seems like a very small drop, but the major part of that drop has been in the 25–34 year old group.

When you look at the exhibit which we presented to you, the red line on the top half of the exhibit shows the 25–34-year age group, the blue line shows the average person. And the bottom half of the exhibit shows the rate of homeownership and the source is the U.S. Census Bureau.

Notice how as that red line at the bottom drops, you have a corresponding rise in the red line above. In other words, without any question, the more difficult it is for the first-time home buyers to get into the act, the less the homeownership rate will increase.

We don't think there's any question that, when you consider the fact that for every dollar spent on new housing, there's an increase of between $7 and $8 in gross national product, and for every dollar spent, there's an increase of between $33–4 in resale, that we think it's a direct relationship to the economy.

But that drop that we've seen since 1980 in the 25–34-year old age group, the principal source of buying, has gone down from 55 percent to 46 percent. That's an 8.7 drop, but a relative drop of almost 15 percent.

That's an incredible drop in only the last 6 years.

We talked about price. Let's talk about down payment. First-time buyers in the United States, on average, put up a down payment of $9,700. A repeat buyer puts up over $32,000. That's a tremendous factor when you consider that most of those repeat buyers are people who have built up their equity and the value of their home and have been able to go out and buy another home.

In California, the average down payment for first time home buyers is $14,500 and $35,000 for repeat buyer. In other words, it becomes more difficult.

How do you get on that ladder?

The fact of the matter is that, in the Federal budget for 1978, housing was 7.4 percent of the total Federal budget. It's gone down to 1.3 and could be under 1 percent in 1988.

A combined total of 900,000 members of our organizations got together and developed a policy toward a national housing policy. And these are our beliefs:

One, decent housing. Two, homeownership is the cornerstone of our free enterprise system. Three, that we need free enterprise and Federal Government involvement and mortgage money.

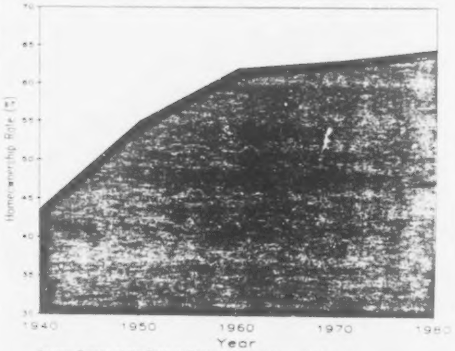
We need a partnership so that people can move up that ladder of housing opportunity.

Thank you very much for the opportunity to be present. I appreciate it and will answer any questions.

[The complete prepared statement of Ira Gribin follows:]

Figure 1

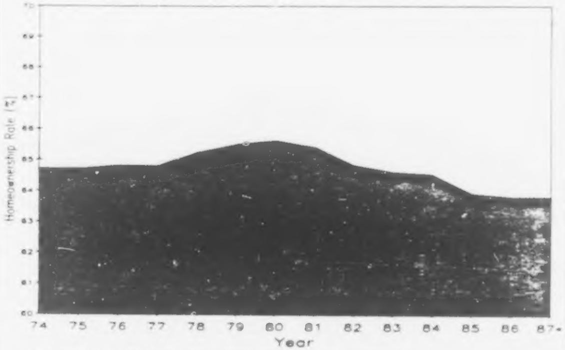
Homeownership Rates, 1940-1980



Source: Bureau of the Census, Census of Population and Housing

Figure 2

Homeownership Rates, 1974-1987



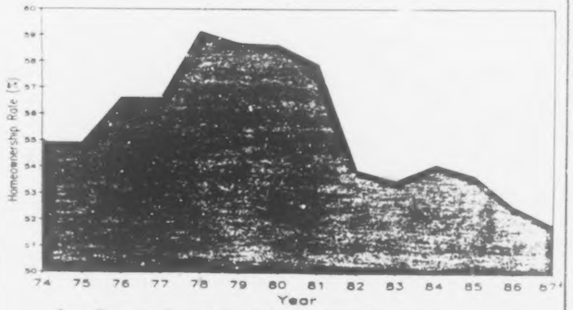
Source: Bureau of the Census, Annual Housing Survey, Housing Vacancy Survey
* First Quarter

Figure 3

Homeownership Rates

Married Couples, Age 25-29

1974-1987



Source: Bureau of the Census, Annual Housing Survey, Housing Vacancy Survey

STATEMENT OF THE
NATIONAL ASSOCIATION OF REALTORS®
BEFORE THE
SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS
SENATE COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
BY
IRA GRIBIN
FIRST VICE-PRESIDENT
JULY 1, 1987

INTRODUCTION

Mr. Chairman, my name is Ira Gribin. I am a REALTOR® from Sherman Oaks, California, and First Vice-President of the NATIONAL ASSOCIATION OF REALTORS®. On behalf of the more than 730,000 members of our ASSOCIATION, I want to thank you and the members of your Subcommittee for the opportunity to present our views on the issue of housing affordability.

Mr. Chairman, I understand that this hearing is first in a series of efforts over the next several months to solicit input and recommendations from the housing industry about potential federal legislative initiatives designed to re-address the need for a federal presence in the housing arena. The NATIONAL ASSOCIATION OF REALTORS® commends you for assuming the leadership in this very necessary endeavor, and we pledge our support and participation as you and your staff work toward the goal of a comprehensive housing bill in 1988.

Let me say that I am also personally delighted to learn that you and your Subcommittee are conducting a field hearing on the affordability issue tomorrow in Los Angeles. I know that my colleagues in the housing industry are looking forward to your visit.

HOUSING: A NATIONAL PRIORITY

Housing has always been and continues to be one of the highest personal and social priorities in America. In recognition of this national expression, the Housing Act was adopted by Congress in 1949 to ensure "decent and suitable" housing for all Americans.

National housing policy emanating from this landmark legislation has traditionally been directed toward two primary goals: providing an adequate supply of affordable housing for all Americans; and promoting widespread homeownership opportunities.

As a nation we must ensure that every citizen has the opportunity to enter the housing arena. Housing should be viewed as a series or ladder of options. The first few rungs of the ladder are steps through rental housing, represented by the homeless up to very low-income, low-income and moderate-income families. Toward the middle of the ladder, first-time homebuyers are represented, with repeat homebuyers moving up the succeeding steps. Regardless of the level on the housing ladder, appropriate policies, incentives and mechanisms must be available to facilitate affordable rental and owner-occupied housing.

Survey data indicate that homeownership still ranks at or near the top of the desires of most Americans. In previous surveys by the Roper Organization, nine out of ten adults under the age 35 regard homeownership as their highest personal priority. And, in the ASSOCIATION's recent "National Homeownership Survey," more than 80 percent of the respondents consistently ranked homeownership as their top choice of 11 "things making up the good life." (REFERENCE EXHIBIT 1)

Homeownership directly benefits society by fostering pride and participation in one's community by encouraging saving and by promoting social and political stability. The ASSOCIATION, and others continue to believe that homeownership deserves a preferred place in our nation's system of values.

Homeownership also benefits the economy because resale and new home purchases contribute substantially to gross national product (GNP) increases in expenditures associated with the home purchase. (REFERENCE EXHIBIT 2)

When an existing or new home is sold, many sectors of the economy benefit from the transaction. A number of business firms benefit from the direct expenditures which take place at the time of the sale, before the sale, and following the sale.

The impact of resales or new home sales on GNP is more evident when one considers the subsequent rounds of spending which occur as businesses and workers take the increased earnings from recent homebuyers' expenditures and spend them on a wide range of goods and services. These secondary and tertiary levels of spending cover a wide range of products and are often diffused well beyond the boundaries of the local community in which the home sale takes place.

For the past 50 years, public policies have been pursued to ensure an effective system for the delivery of housing to all Americans, and significant progress has been made toward achievement of this goal. The tremendous housing needs that faced the nation in the 1930s and the war years have been alleviated by a combination of robust economic growth and successful federal policies. These gains have brought the country much closer to its housing goals and resulted in a steady rise in the nation's homeownership rate from 44 percent in 1940 to over 65 percent in 1980.

However, in the past several years, housing policy has been victimized in the debate over the proper size and function of the federal government. The result has been a decline in the share of the nation's resources directed toward housing. For example, housing's share of the federal budget has declined. Budget authority for the Department of Housing and Urban Development (HUD), which accounted for 7.4 percent of the total federal budget in 1978, is estimated to be less than 1 percent in 1988. (REFERENCE EXHIBIT 3 AND TABLE 1).

The impact of these policy shifts are already being felt in terms of housing affordability problems and declining homeownership rates. The NATIONAL ASSOCIATION OF REALTORS® is very concerned about the affect that this growing trend will have on the ability of our citizens to climb the housing ladder. For, without reaching that first rung, there is little hope of attaining the ultimate goal of homeownership.

In the remainder of this statement, I will outline the nature and extent of the affordability problem. I will also discuss the importance of the federal government's role in addressing this important issue through the development of a positive and comprehensive NATIONAL HOUSING POLICY.

DECLINING HOMEOWNERSHIP RATE

A decline in overall homeownership rates from 1980 to 1986 has signaled a reversal of the long-time trend of growth in this area. This general decline represents the first sustained one of its kind since the 1930's.

In general, this reversal can be attributed to home prices, which have risen faster than income in recent years, increasing buyer difficulty in meeting downpayment and closing costs and higher mortgage payments.

Specifically:

- Real income has increased only 7 percent since the 1970's, while real home prices have risen 32 percent. This relationship can be measured by the ratio of existing single-family median home prices to median family income. (REFERENCE EXHIBIT 4)
- The actual decline in homeownership rates from 65.6 percent of households in 1980, to 63.8 percent in 1986 represents a 2.7 percent change. (REFERENCE EXHIBIT 5)
- Based on the ASSOCIATION's data, it can be estimated that there are almost 1.5 million fewer homeowners today than there would have been if the 1986 homeownership rate had attained the 1980 level.

In states which have relatively high housing costs, the drop in homeownership has been even more dramatic. For instance, in my home state there was a 5.6 percentage point drop in the homeownership rate from 1980 to

1986, compared to the 2.7 percentage point drop experienced by the nation as a whole. Moreover, because housing prices are higher, the rate of homeownership is lower--only 53.2 percent in California in 1986. This decline represents the aftermath of the on-going crisis in housing affordability.

HOUSING AFFORDABILITY

I'd like to take a moment to review some of the fundamental factors behind the housing affordability problem.

There are a variety of methods available to measure housing affordability. These include: (1) the ratio of current housing expenses to current household income, (2) the ratio of median sales price to income, and (3) the percentage of households able to purchase the median priced home. Whichever measure is used, there are three primary factors affecting housing affordability that need to be examined: housing prices, income, and mortgage interest rates.

Several years ago, the NATIONAL ASSOCIATION OF REALTORS® began monitoring the affordability of housing by developing a Housing Affordability Index. The index includes the median prices of resale homes and mortgage interest rates and compares the resulting mortgage payment on an 80% loan to the ability of the median income household to carry the loan.

Under the index, housing was most affordable in 1972 when the median income family had an income nearly 55 percent above the minimum required to carry the mortgage. From that point, affordability declined consistently, hitting bottom in 1982 when the median income family had less than 70 percent of the income required to carry a standard mortgage on the median priced home.

generally declining mortgage rates after 1982 combined with moderate home price increases to allow the index to rise by approximately one-third over the period between 1981 and 1986.

While the ASSOCIATION's index indicates that affordability has increased, it does not reflect the fundamental problems which exist in the first-time homebuyer segment of our population. As I will discuss in more detail later, first-time homebuyers, typically adults in the 25- to 34-year old category, face the most difficulty in realizing the goal of homeownership. As evidence of this growing trend, I'd like to point out the correlation between the decline in the home price-to-income ratio for first-time homebuyers, and the overall, decline in the homeownership rate. (REFERENCE EXHIBIT 4)

As a measure of affordability, the decline in the home price-to-income ratio means that the "typical" first-time homebuyer is unable to purchase the "typically" priced home.

Rising Home Prices

Home prices have increased quite rapidly in recent years. For the U.S. as a whole, the median priced existing single-family home in 1970 was $23,000. By 1986, the median priced home had risen to $80,300—a 249 percent increase! In California, the increase is far higher due to a combination of a high level of demand and tight supplies, as building activity has been constrained by high land costs and anti-growth measures. As a result, the median priced existing single-family home in California shot from $24,300 in 1970 to $131,500 in 1986—a 441 percent increase!

Mr. Chairman, California is not the only place where housing prices have sky-rocketed. Unfortunately, reliable statistics are not available for most areas prior to 1982. However, nationwide housing prices have jumped 21 percent in the last five years. In many places this national rate of increase has been surpassed by a large margin. In the New York/Northern New Jersey/Long Island metropolitan area, where nearly 18 million Americans live, home prices have more than doubled in the last five years. Similarly, in greater Boston, the median home price has doubled in the last four years alone. Home prices have also increased by at least 50 percent in the last five years in the Hartford, Providence, Albany, Rochester and Syracuse metropolitan areas.

Incomes Have Not Kept Pace

Incomes over this time increased too, but not as rapidly. According to the U.S. Bureau of the Census, "Current Population Reports," median family income in the U.S. over the same 1970 to 1986 period increased only 183 percent from $9,867 to $27,893, compared to the corresponding 249 percent increase in housing prices. Over this period, California experienced comparable income growth, with median family incomes rising from $10,828 in 1970 to $30,837 in 1986. In comparison to the 441 percent jump in California housing prices, income growth has lagged woefully behind.

While the changes are somewhat less dramatic when you look at changes during the 1980s, clearly many communities continue to have housing costs increasing much more rapidly than local residents can absorb. In the Boston area, for example, home prices have doubled in the the last four years, while the median family income has increased by one-third as much.

Not only high-cost cities suffer this problem either. In the Kansas City area in the last five years, home prices have increased by 47 percent while incomes have increased by only 38 percent.

Volatile Mortgage Interest Rates

Because financing plays such a crucial role in the purchase of a home, it, too, is a major factor which impacts housing affordability. Mortgage interest rates--the most volatile factor--injects a degree of uncertainty and instability into the housing affordability picture. During the first half of the 1980s, interest rates soared in response to a shift in Federal Reserve Board policy from one of controlling interest rates to one of controlling the money supply and allowing rates to "float". As a result of the subsequent cut back in monetary growth, interest rates peaked in 1982 at levels as high as 17 percent, causing housing to suffer its worst downturn since World War II.

While the decline in interest rates during 1985 and 1986 helped boost housing affordability, the long-term increase in housing prices as compared to income growth remains a real threat to recent gains. If housing affordability is measured by the ratio of housing expenses-to-income, then housing affordability in the U.S. has worsened from a burden of 20.3 percent in 1970 to 26.7 percent in 1986. And, for high cost regions, the situation is far worse. California's housing expenses-to-income ratio, for example, has

increased from 21.1 percent in 1970 to 39.3 percent in 1986.

There is also evidence that affordability will continue to be a problem in the future when the incomes of renters and homeowners are compared. Census data show that the 1980 median annual income among renting households was $10,500, or only 53 percent of the $19,800 median among homeowning households. Renters not only have lower incomes than homeowners, in general, but the income of renting households has been rising more slowly than that of homeowning households. From 1970 to 1980, median incomes rose 66.7 percent among renters but 104.1 percent among owner occupants. While part of this gap was caused by the shift of some renters to homeownership between these two periods, it does not speak well for homeownership trends in the future as more and more renters find that their income growth fails to keep pace with the rising costs of homes.

AFFORDABILITY AND FIRST-TIME HOMEBUYERS

Aside from the home price, income and financing constraints faced by prospective homebuyers, there is also the question of a buyer's ability to make the required downpayment. Those who already own a home and sell it to buy another, have enjoyed home value appreciation and can use this gain as the downpayment on another home. For those who purchased before the huge rise in housing prices which began in the mid-1970's, these gains may be substantial, and repeat buyers can often avoid the increasing wealth constraints to housing affordability.

First-time homebuyers, however, are not so fortunate. It is this segment of our population, Mr. Chairman, who face increasing barriers to realizing their goal of homeownership who we are most greatly concerned about. It is to this area that the ASSOCIATION asks the Subcommittee to give particular attention.

Prospective first-time homebuyers tend to face both downpayment and income constraints. They are, most often, younger households who have yet to accumulate substantial savings for a downpayment and are at the lower end of their income earning curve. Data collected by both the NATIONAL ASSOCIATION OF REALTORS® and the CALIFORNIA ASSOCIATION OF REALTORS® provide evidence of the difficulties faced by first-time homebuyers.

All around the country, first-time homebuyers purchase significantly less expensive housing than repeat buyers--$79,800 compared to $125,400 in 1986. We also see this in California where first-time homebuyers' average purchase is $112,950 compared to $149,900 for repeat buyers. Nationally, first-time homebuyers also have lower annual incomes; $35,500, compared to repeat buyers who typically earn $51,900 per year. In California, first-time buyers' incomes average $39,996 compared to repeat buyers who earn, on average, $50,000 a year.

On the national level, first-time buyers average lower sales-price-to-income ratios, purchasing housing valued at 2.25 times their income compared to 2.41 times recorded for repeat buyers. Average lower sales-price-to-income ratios are also reflected in California, with first-time homebuyers purchasing housing valued at 2.8 times their income, as opposed to 3.0 times income recorded for repeat buyers.

In addition to purchasing less expensive homes, first-time buyers make significantly smaller downpayments than repeat buyers. On a national basis, first-time homebuyers' downpayments were significantly less, averaging $9,700,

compared to repeat buyers' average downpayments of $32,100. California data indicates that first-time buyers' downpayments averaged $14,550 compared to $35,000 for repeat buyers. Across the country, median loan-to-value ratios for the first-time buyer segment amounted to 93.6 percent, as opposed to 80 percent for the repeat buyer category. Median loan-to-value ratios among first-time buyers in California registered 88.4 percent compared to 78.2 percent for repeat buyers.

Affordability problems confronting first-time buyers are also reflected in the types of housing they purchase. Compared to repeat buyers, the first-time buyer is more likely to purchase a smaller home with fewer bedrooms, and is more likely to purchase a condominium as opposed to a single-family detached home.

What all this data on first-time homebuyers means, Mr. Chairman, is that this part of our population is being severely restricted by the market, and that they are effectively under-housed because of their inability to purchase the typically price home. Furthermore, as a group, potential first-time homebuyers represent the most serious threat to housing markets. The homeownership rate of 25- to 34- year olds in 1985 was 46.3 percent of households, a decrease of 8.7 percent from the 1980 level of 55 percent.

Although the problems of affordability have been, and will continue to be a problem with younger first-time home purchasers, there is good evidence to suggest that the magnitude of these problems will be reduced by the aging of the population. We believe this because a variety of demographic and cultural changes are combining to alter the age profile of the U.S. population.

In general, over the last three decades there has been a substantial proportional increase in the number of single-person households in the prime homebuying years. In 1950, only 9.1 percent of households were headed by a single-person; but, by 1986 almost 24 percent were one-person households. Single-person households in the 25 to 44 age range increased from 2.2 percent in 1960 to 7.3 percent of all households in 1985. Moreover, single-person households aged 45 to 64 remained a relatively constant proportion, rising from 5 percent in 1960 to 5.8 percent in 1985.

Assisting this trend has been changes in economics and social attitudes over the past couple of decades. Greater access to education and attitudes toward cohabitation and divorce have increased the likelihood that younger people will postpone forming traditional relationships which have tended to lead naturally to homeownership. Coinciding and interacting with these sociological changes have been the economic problems of rising interest rates and home construction costs. Moreover, median household incomes have risen somewhat more slowly than median home prices, putting a cash squeeze on new homeowners. In fact, this inability to get into the homeownership circle may be causing many younger households to spend their money on more attainable things, giving-up on the savings discipline one must develop to be able to afford a home. Indeed, the personal savings rate has dropped dramatically over the last couple of years so that now, at 3.8 percent, it is at the lowest rate since 1947. (It was 6.3 percent in 1984.)

Nevertheless, one of the blessings of age is that we become more willing to put down roots and make the economic sacrifices necessary to carry us through the latter part of adulthood. Furthermore, as we age, it becomes

important to find someone to help share the burdens and to provide us with a sense of history and future purpose. Thus, with the maturing of the post-war "baby boom" generation it is expected that we will see a return to more traditional values. There are some hopeful signs already--birth rates are starting to inch-up and divorce rates have been declining. Although it may take a while, if past history is any indication, these events should help place further pressure on the desire for homeownership.

RISING INTEREST RATES EXACERBATE AFFORDABILITY PROBLEMS

A rise in interest rates is immediately reflected in higher costs of homeownership. An increase in the mortgage rate has a similar impact on the ASSOCIATION's Housing Affordability Index. A mortgage rate one point higher than the average last year would have reduced the affordability index by several points, a decrease that means the median income family would either have to increase the downpayment or purchase a less costly home.

The CALIFORNIA ASSOCIATION OF REALTORS® has estimated that when interest rates rise from 9 percent to 11 percent there is a 7 percentage point drop in the proportion of California households which can afford to buy the median priced home in the state, falling from 35 percent to only 28 percent. This assumes that a 20 percent downpayment can be made and that the median home price stays the same. If these percentages are applied to the number of households in the state, approximately 9.7 million, then the number which could afford to buy the median priced home would drop from 3.4 million to 2.7 million. In other words, 700,000 fewer households can afford to purchase when interest rates jump 2 percentage points between 9 and 11 percent.

IMPACT OF DEMOGRAPHIC TRENDS ON FUTURE AFFORDABILITY

Another demographic trend which will impact affordability in the future is the changing ethnic composition of the population. This is of particular importance in states such as California, where the ethnic composition is changing rapidly due to the influx of immigrants from Latin America and Asia. For example, in the year 2000, the California Department of Finance has projected that the percentage of residents of Hispanic origin will be 26.6 percent compared to 21.2 percent in 1985. Further evidence shows that for the Hispanic population, their median family income was over $5,000 below that of the rest of the state's population at the time of the census in 1980. Furthermore, their homeownership rate was only 42.4 percent compared to 58.8 percent for the state as a whole in 1980.

California is not the only area to experience the impact of these trends. Other states have and will continue to face pressures resulting from rapidly changing demographics. These growing developments throughout the nation require prompt and innovative response from public policy makers to ensure that adequate housing is available to meet this increasing market demand.

AFFORDABILITY IN THE RENTAL MARKET

The affordability problem is not, of course, confined to homeownership. As we mentioned earlier, the provision of adequate and affordable rental housing is an essential part of the housing arena, and an area which we feel the federal government's role is paramount.

The affordability problem in the rental market has been particularly intensified by adoption of the Tax Reform Act of 1986 which seriously cut back incentives to invest in rental housing. We believe that this withdrawal of incentives will cause shortfalls in housing supply, causing rents to rise substantially over the next few years.

As a result of the environment created by adoption of these new tax laws, we estimate that rents will rise by $540 per year or 13 percent over pre-tax law levels. Rents will have to rise 10 to 16 percent or between $35 and $56 for an additional annual payment of between $420 and $672. For the typical renter, this represents an additional rent burden of between 3 and 5 percent of income. And, while renters tend to be non-itemizers and so would benefit from the reduced federal tax burden under the Tax Reform Act, the annual decline in federal taxes for a taxpayer at this income level would be in the range of $400 to $500. For the typical renter, the reduced tax burden would be completely absorbed by eventual rent increases.

Affordability is particularly acute for low-income renters. According to data supplied by the Department of Housing and Urban Development (HUD), a substantial majority of households with incomes below $10,000 and more than one-third of those with incomes between $10,000 and $15,000 pay more than 35 percent of their income for rent.

The number of these households and their rent burden has been growing rapidly at the same time that federal efforts to enhance the availability and affordability of rental housing has slowed. Although the private sector has been able to meet some of these needs, recent tax changes, which we discussed earlier, further reinforce the need for ongoing involvement by all levels of government.

Federal funding for the various assisted housing programs has decreased by almost 70 percent from the FY1980 levels to FY1986. The resulting decline in funding for federally-assisted housing, combined with other market developments like demolition of inexpensive housing, gentrification, and general increases in real rents have brought about an overall reduction in the number of low-cost rental units.

According to the National Association of Home Builders report, "Low- and Moderate-Income Housing: Progress, Problems, and Prospects," there were 10.8 million units renting for less than $250 per month in 1974 (1983 dollars). By 1983, the number of units renting for less than $250 per month had fallen to 8.8 million.

Projected conversions of federally-assisted section 236 and Below-Market Interest Rate (BMIR) units to market-rate rental units may also contribute to a reduction in affordable low-income housing.

This affordability problem in the rental market may also negatively affect the increasing homeless situation across the country.

Although the ASSOCIATION has ongoing concerns about the federal budget deficit, the appropriate role of the federal government in this area requires, we believe, a unified reexamination.

GEOGRAPHIC AREAS OF SIGNIFICANT AFFORDABILITY PROBLEM

Certain areas of the country face more serious affordability problems than others. Such areas include Boston, Orange County in California, the greater New York area, Hartford, San Diego, the San Francisco Bay area in California, and the greater Washington, D.C. area, among others. Unfortunately, it is

usually the dynamic metropolitan areas which suffer the most, as their economies generate job opportunities and workers seek housing in the near vicinity. The demand for housing in these areas, most of which are already significantly built up, pushes prices higher, making it increasingly more difficult for workers to buy a home within reasonable commuting distances from their jobs. In some areas the problem is so severe that companies which are considering a particular area for expansion or relocation become discouraged by significantly higher housing costs.

To illustrate the severity of the problem, I'd like to use my home state as an example. In the state as a whole, only about one-third of the households could afford to buy the median priced home in 1986. In the San Francisco Bay area, only 17 percent of the residents could afford to buy the median priced home there, which was over $160,000. Likewise, in Los Angeles, only 29 percent could afford to buy the median priced home in that area which was almost $129,000. With the median prices of homes at over $159,000 in Boston, over $160,000 in the New York/New Jersey/Long Island area, and $129,000 in Hartford, the affordability problem also exists in these areas.

Economically depressed areas also typically face severe affordability problems. Certain regions of the country, principally the energy-sensitive states, which were prepared for a boom when the bottom fell out of oil prices, have tracts of homes sitting vacant with no buyers in sight. With jobs very difficult to find, the residents of these areas have no way of earning the income necessary to purchase these homes, so they sit unused or new owners are forced to walk away because they cannot make payments on their mortgages.

ADDRESSING THE PROBLEMS OF AFFORDABILITY: A NATIONAL HOUSING POLICY

The problems we have alluded to in California and the rest of the country result substantially from the absence of a clearly defined housing policy for our nation. We feel the problems of affordability for both renters and owners must be addressed through policies that are national in scope and provided in a consistent framework.

The NATIONAL ASSOCIATION OF REALTORS®, in conjunction with the National Association of Home Builders, and the Mortgage Bankers Association of America recently submitted to the President and Congress the framework for a NATIONAL HOUSING POLICY that will, once again, recognize the high priority assigned by the American people to decent housing for all and widespread opportunities for homeownership. This document highlights the importance of the federal government's role in helping to promote these housing goals and stresses the need for coordination of the many elements that form an effective housing policy. The basic principles underlying the document are:

- Homeownership is the cornerstone of our democratic system of government.
- Every individual should have the opportunity to live in decent and affordable housing.
- The free enterprise system and competitive markets are a principal source of affordable housing.
- Maintaining low, real interest rates is essential for the provision of affordable housing.

From these principles we go forward to establish the bounds of appropriate policy responses in a number of component areas. I would like to briefly touch upon the directions national policies should take in several areas related to the problems of affordability for rental and owner-occupied housing.

Housing Finance

Any discussion of housing affordability must also consider the availability and cost of housing credit. It is essential that the housing finance system established over the years be maintained and strengthened in the future. To accomplish this goal, we recommend federal action to:

- Preserve and strengthen the federal primary loan insurance and guarantee programs, FHA and VA, which serve moderate-income and first-time homebuyers. Furthermore, resist all efforts to privatize, restrict, or encumber the operation of these programs.
- Maintain the valuable role of the federally-sponsored secondary market institutions, Ginnie Mae, Fannie Mae and Freddie Mac.
- Foster the continued development of mortgage-related securities and encourage all levels of government to remove legal or regulatory impediments to investment in these securities.
- Promote a viable system of thrift institutions backed by a strong Federal Home Loan Bank System and a revitalized FSLIC.
- Promote the flow of funds into housing from private sources, including commercial banks, life insurance companies, pension funds and foreign investors.

- Facilitate owner-financing as an affordable means of supplementing institutional credit markets.

THE NATIONAL ASSOCIATION OF REALTORS® supports maintaining and strengthening the federal primary loan insurance and guarantee programs. The FHA insurance program should remain as it is presently constituted and current premium, eligibility and assumability features should not be altered. Legislation guaranteeing the operation of the program without interruption (e.g., permanent authorization), and appropriate actions to improve the efficiency and processing time of the program through private sector involvement, are highly desirable. The ASSOCIATION recognizes that Congress has favorably addressed many of these issues, and the REALTORS® I represent commend your leadership and action in this important area.

Similarly, the VA program should be maintained as a program designed to maximize homeownership opportunites for all veterans. Correspondingly, veterans should continue to be permitted to finance loan origination and VA processing costs without restrictions. With this goal in mind, increased user fees would be contrary to the public interest and should be statutorily restricted. An important affordability-related consideration is that both the FHA and VA programs should have appropriate loan, or loan guarantee limits. These must reflect local housing price differences and be responsive to changes in housing costs.

The NATIONAL ASSOCIATION OF REALTORS® also supports a strong secondary mortgage market because it has greatly increased the availability of mortgage capital and reduced homeownership costs for millions of Americans.

The federal and federally-sponsored secondary market institutions, Ginnie Mae, Fannie Mae, and Freddie Mac, represent the principal foundation, for these activities. These institutions provide nation-wide access to residential mortgage credit at a uniform cost, and at all stages of the credit cycle.

For these reasons, we strongly oppose any attempt to "privatize" or weaken Fannie Mae or Freddie Mac. Although developing rapidly, private sector substitutes for these federally-related institutions are not yet in a position to meet the homeownership needs of first-time and moderate-income families. Moreover, the counter-cyclical role of Fannie Mae would be jeopardized by the substitution of a purely private entity operating without federal charter.

Homeownership Incentives For Moderate-Income Families

While the 1986 Tax Reform Act left most of the tax incentives for owner-occupied housing intact, these alone are not sufficient to resolve housing affordability problems for families at moderate-income levels. Additional incentives are necessary, such as tax-exempt Mortgage Revenue Bond (MRB) and Mortgage Credit Certificate (MCC) financing, to provide assistance for low-income and many moderate-income, first-time buyers. This type of financing is essential to state and local initiatives to enhance homeownership affordability.

Tax-related incentives also are needed to help first-time buyers meet rising downpayment requirements. We specifically recommend that:

- MRB financing should be expanded in volume and continued beyond the current law sunset in 1988.

- Tax credits under the related MCC program should be made refundable.
- First-time buyers should be permitted to withdraw, without penalty, limited amounts from IRA or 401(k) tax-deferred savings accounts for the downpayment on their homes.

Incentives for Rental Housing

As we mentioned earlier, in the area of rental housing, tax incentives have been a critical factor in motivating private investors to settle for a lower return from rents and to take on the extra difficulties of providing rental housing for persons with low- or moderate-incomes. Before the Tax Reform Act of 1986, the primary incentives for low-income housing consisted of tax exempt multifamily rental housing bonds, rapid depreciation schedules and special deductions for construction period interest and taxes. Congress felt that these general benefits operated in an uncoordinated manner, and failed to guarantee that affordable rental housing will be provided to low-income individuals.

As a result, a new tax credit was enacted, which could be claimed over a 10-year period, for certain expenditures on low-income units. While this credit was noble in spirit, as originally enacted, the program was somewhat unworkable in practice.

Fortunately, the "technical corrections" legislation to the tax bill proposed several changes which improve the workability of the low-income tax credit. The principal improvement appears to be a provision which will allow developers to set the value of the credit when the contract is signed rather

than when the structure is placed in service. We look forward to further improvements in the credit, as they become apparent and hope that Congress will extend authority for the credit beyond its scheduled 1989 "sunset" date.

We also recommend that reasonable standards be provided for state and local government usage of multifamily industrial development bonds. This vehicle is an important tool for the development of affordable low- and moderate-income rental housing.

STATE AND LOCAL EFFORTS FOR AFFORDABLE HOUSING

Competition for economic development has forced states and cities to find new approaches for helping to make housing more affordable, as the federal government has withdrawn much of its long-time support to this vital sector. While a strong federal presence is still seen as an essential component in meeting the goal of housing affordability, local governments have been seeking new approaches to this problem.

These partnership arrangements for low- and moderate-income housing generally have been based upon some form of federal assistance--particularly tax provisions and grants. However, the state or local governments have not only served as conduits for federal assistance, but also have provided regulatory relief, property tax abatement, donations of land, and assistance from general government funds or designated revenue streams.

We believe that each state and locality should address the housing needs of its lower-income or otherwise disadvantaged citizens to the extent possible. However, inasmuch as Congress has stated that housing affordability is a national concern, the federal government must continue to provide financial tools to back state and local efforts. These tools include tax-exempt financing, the new low-income housing credit, and certain direct grant programs.

Also, housing affordability is directly affected by state and local, regulation of the housing industry. Excessive and unnecessary regulation drives up the cost of new housing and ultimately makes homeownership less affordable. As a consequence government at all levels should be encouraged to:

- Eliminate regulatory barriers and fees which unnecessarily reduce the affordability of housing, such as impact fees, growth moratoriums, and excessive zoning restrictions.

STATE INITIATIVES

In the past, different states have adopted varying approaches to the problem of housing affordability. State and local participation in mortgage revenue bond programs helps to reduce the cost of homeownership. About a dozen states, including my home state, have been active in promoting mortgage credit certificates (MCCs) to assist low- and moderate-income first-time homebuyers. As you know, MCCs allow a credit against federal income taxes for the specific purpose of buying a home. Lenders view this credit as additional income and are, thus, able to lower the income level required for a borrower to qualify for a loan.

The state of Michigan was the first in the nation to implement this program. Its MCCs are now approaching a volume of $50 million in what was originally thought to be an experimental program. The certificates have been servicing households with, on average, incomes of $22,000. Effectively, MCCs can lower the interest rate by as much as 2.5 points. The program is now operative through 80 Michigan lenders.

In my own state of California, the capital city of Sacramento became the first local government in the state to adopt the program. The Sacramento Board of REALTORS® worked closely with the city's Housing and Redevelopment Agency to make the dream a reality. Initial authorization was granted in December 1985, and the program began operation in the third quarter of 1986 with $11 million.

The response was overwhelming. By March, 1987, 20 to 30 new residential requests were being received daily. In 4 months, the number of participating lenders increased from 10 to 30. As of April, 1987, over 500 MCCs have been awarded or are pending. The average household income of those applying for the program is $26,213; the average mortgage loan amount if $69,985. A second allocation, this time for $15 million has been approved, and new authorization for 1987 has been requested.

It should be noted that MCCs are generally used on existing single-family homes in conjunction with FHA or VA financing. Since first-time homebuyers with moderate-incomes generally have difficulty meeting downpayment and qualification requirements, the supplemental benefit provided by MCCs makes them exceptionally useful.

The success of these valuable state-initiated programs is, however, threatened because the mortgage revenue bond program is scheduled to expire on December 31, 1988. In addition, under the Tax Reform Act of 1986, mortgage revenue bonds and multi-family industrial development bonds are included under a single volume limit for all qualifying private activities. The new volume limit will sharply reduce the volume of bonds which can be issued, particularly in states such as California, which have been active users of their mortgage revenue bond authority.

California has also developed an interest rate buydown program to help make housing more affordable to first-time homebuyers. This program has enabled several thousand California families to realize the dream of homeownership.

PUBLIC/PRIVATE PARTNERSHIPS

A large number of states and cities have established public/private partnerships, using contributions from foundations and other sources to help non-profit groups build housing. Business and industry have, themselves, recognized the need and are attempting to fill the gap between the public and private sector.

One of the most effective examples of this effort is BRIDGE, the Bay Area Residential Investment Development Group, a non-profit organization based in San Francisco. Founded in the early 1980's, this program was the brainchild of a number of major corporations, concerned by the need to attract employees to a high-cost area. BRIDGE combines the resources and expertise of business, government, and philanthropy to produce large volumes of quality homes for Bay Area families who earn between $12,000 and $25,000 per year. Since it began active operation in 1983, it has participated in the development of over 2,400 units valued at over $200 million. More than $5 million has been added to an initial gift to provide working capital for BRIDGE.

THE NEED FOR COOPERATION FROM ALL LEVELS OF GOVERNMENT AND INDUSTRY

While federal support of housing is a critical element in meeting the goals of decent housing for all and widespread homeownership opportunities, these will only be achieved if there is mutual support and cooperation from all concerned groups, including state and local governments, private enterprise, charitable organization, as well as the REALTORS®, builders and those involved in mortgage financing. With widespread cooperation, efforts towards making housing more affordable will be more effective.

It is toward the federal government that we turn to guide our efforts and to support us in those areas which cannot be sustained at the state and local levels. Although my testimony here today has narrowly focused on affordability for renters and owners, we have offered our joint housing policy document as an agenda to address a broad spectrum of housing issues such as housing finance; tax policy; the cost and availability of low- and moderate-income housing; and a variety of other issues. Toward this end, a renewed commitment to housing must be taken by the federal government, to ensure an effective system for the delivery of affordable housing to all Americans.

CONCLUSION

Thank you again Mr. Chairman, for the opportunity to participate in this worthwhile hearing. The NATIONAL ASSOCIATION OF REALTORS® looks forward to working with you and your staff in the weeks ahead as you examine the critical problem of housing affordability and develop appropriate solutions.

I will be happy to answer any questions.

1502r

TABLE 1

HUD And Total U.S. Government
Budget Authority: 1977-1987 and 1988 Proposed
($s in Millions)

Year	HUD Budget Authority	Total U.S. Budget Authority	HUD As a % of Total
1977	33,818	472,654	7.15
1978	37,994	512,434	7.41
1979	31,142	569,634	5.47
1980	35,852	676,695	5.30
1981	34,220	745,887	4.59
1982	20,911	809,854	2.58
1983	16,561	888,082	1.86
1984	18,148	949,921	1.91
1985	16,682	1,059,763	1.57
1986	15,928	1,072,773	1.48
1987	15,200	1,093,933	1.40
1988p	10,229	1,142,180	.90

Note: p--Proposed
Source: Historical Tables, Budget of the United States Government, Fiscal Year 1987, Executive Office of the President, Office of Management and Budget.

Exhibit 1

THINGS MAKING UP THE "GOOD LIFE"

(Percent Indicating Part of "Good Life")

Top Five Choices	All	Owners	Renters
A home you own	85	92	76
A car	84	88	78
A happy marriage	79	81	75
An interesting job	78	78	79
A yard and lawn	76	82	68

Source: REALTORS National Homeownership Survey, Nov. 1986

Exhibit 2

ESTIMATING THE CONTRIBUTION OF RESALE AND NEW HOMES TO GNP

The resale and new home markets are important to GNP because home sales contribute substantially to GNP increases in expenditures associated with the home purchase.

When an existing or new home is sold many people gain from the transaction. Buyers and sellers benefit by moving into homes which better suit their current needs; and, mortgage lenders and real estate practitioners gain from the transaction. In analyzing the impact of these transactions, it is useful to examine the expenditures associated with homebuying—those that take place at the time sale, before the sale and after the sale.

Expenditures at Time of Sale

A number of business firms benefit from the direct expenditures which take place at the time of the home sale. These businesses include: household movers, attorneys, real estate appraisers, termite inspectors and structural inspection firms, surveyors, property insurance and title insurance companies, and the local governments which earn fees and taxes on the transaction. On average, these expenditures will total about $9,000 for each resale transaction in 1985, and $5,800 for each new home sale. These numbers were derived using results from the 1979 Survey of HUD-1s as was required under the Real Estate Settlement Procedures Act of 1978. National statistics were generated by HUD of costs at the time of residential sale, and NAR estimates were made from this data.

Expenditures Before the Sale

In calculating the contribution to GNP of a resale transaction we should not overlook the expenditures that are made by owners immediately prior to putting their home on the market. Since home sellers strive to present their home in the best possible light, many repairs and clean-up jobs that may have been postponed are done just before the house is placed on the market. Local merchants and contractors receive income from these expenditures, in particular: painters, hardware and building supply stores; carpenters; roofing, plumbing, and electrical contractors; lawn service companies and gardeners; carpet and drapery cleaners; heating and cooling contractors; and appliance repair services. Typically these expenditures will average $950 for each resale in 1985. Analysis of Bureau of Labor Statistics (BLS) data on consumer expenditures was used to make these estimates.

Expenditures After the Sale

There is also a strong relationship between buying a new or existing home and the subsequent purchase of additional goods and services. In the months following a home sale transaction, homebuyers outspend non-mover homeowners by a substantial amount. These after-sale expenditures range from major capital improvements and the purchase of furnishings down to the purchase of numerous smaller household and yard items. Analysis of BLS consumer expenditure tapes used to construct the Consumer Price Index identified seven categories of goods and services in which recent buyers outspend non-mover homeowners:

- Non-recreational household furnishings (furniture, linens; minor and major appliances; etc.)
- Capital improvements (building or modernization of rooms, garages, or wings; construction of patios, driveways, or walkways; plastering or paneling improvements; heating or air conditioning improvements, etc.)
- Miscellaneous consumption (telephone service; service and maintenance contracts, etc.)
- Recreational household furnishings (stereos, television, radios, etc.)
- New vehicles (automobiles and trucks)
- Clothing
- Insurance and pensions

Overall, homebuyers in 1985 will have outspent non-mover households by $1,900 for resale homes and $2,150 for new homes within the 12 months immediately following a home purchase.

The Multiplier Effects Are Substantial

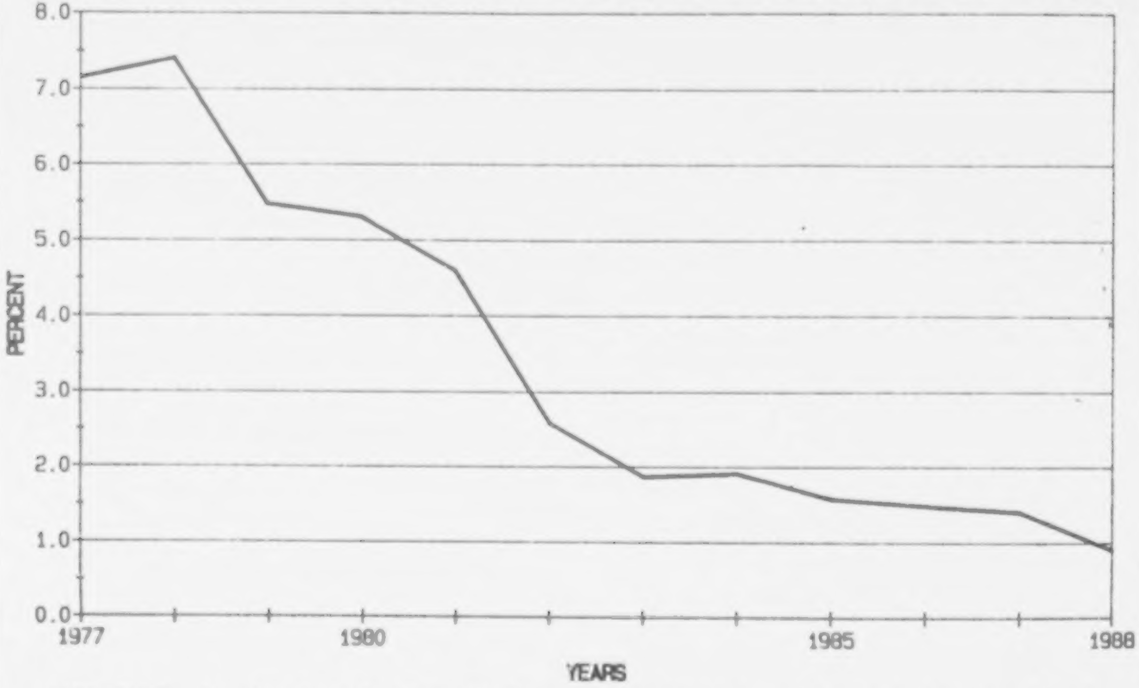
The impact of resales or new home sales on GNP is even more evident when you consider the subsequent rounds of spending which occur as businesses and workers take the increased earnings from recent homebuyers' expenditures and spend them on a wide range of goods and services. These secondary and tertiary rounds of spending cover a wide range of products and are often diffused well beyond the boundaries of the local community in which the home sale takes place. In 1985, these additional rounds of expenditures will total about $6,207 per existing home, and $37,539 for each new home sold. A major portion of the new home multiplier effect is due to the multiplier effects of the initial construction expenditures.

Total Contributions to GNP Per Transaction

On a per unit basis each 1985 resale will result in almost $12,413 of direct expenditures and over $6,207 of secondary expenditures. Each new home sale in 1986 will result in $75,078 direct expenditures and $37,539 in multiple expenditures. Together, these expenditures will contribute over $18,000 for a resale and $112,600 for a new home sale to GNP.

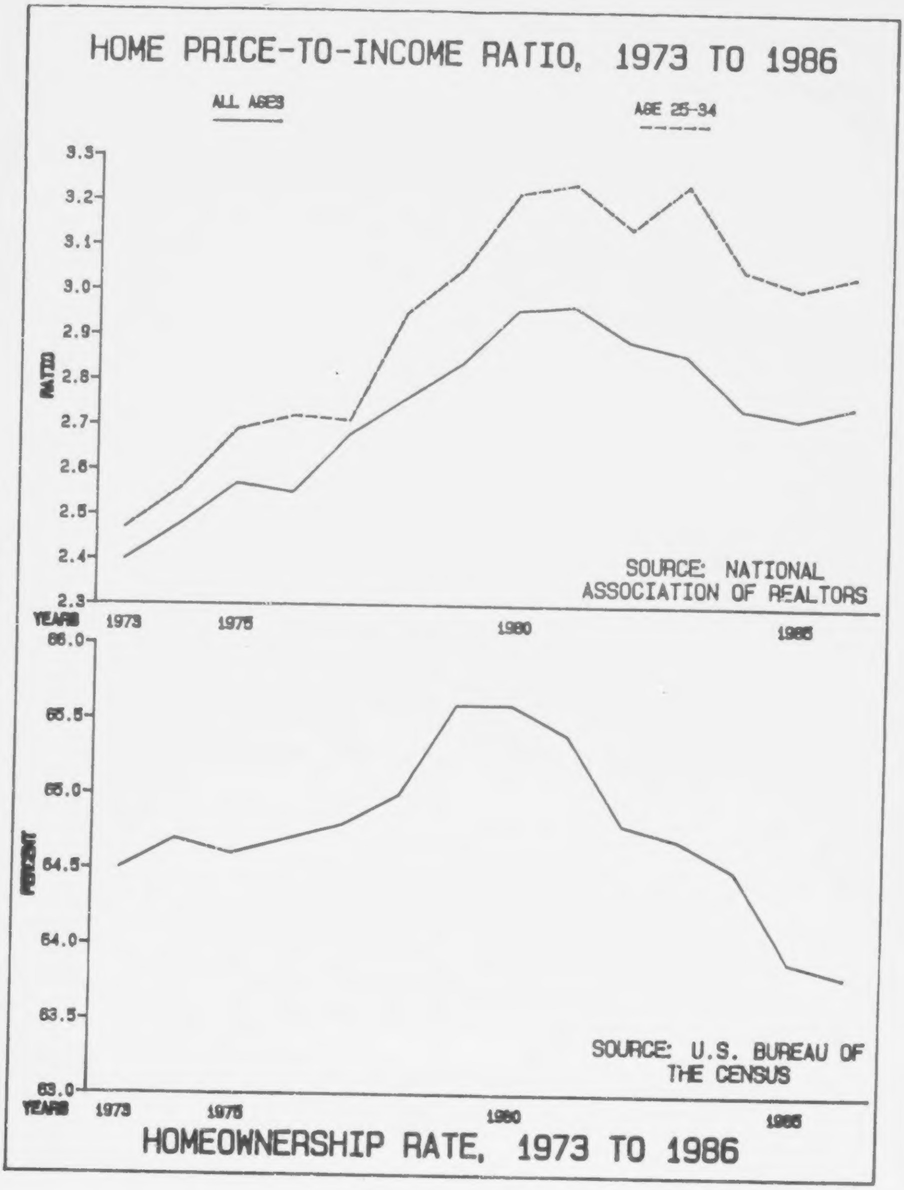
Exhibit 3

BUDGET AUTHORITY OF HUD
PERCENTAGE OF THE TOTAL FEDERAL BUDGET, 1977-1988



SOURCE: Budget of the U.S. Government, Fiscal Year 1988

Exhibit 6



HOME PRICE-TO-INCOME RATIO, 1973 TO 1986

SOURCE: NATIONAL ASSOCIATION OF REALTORS

SOURCE: U.S. BUREAU OF THE CENSUS

HOMEOWNERSHIP RATE, 1973 TO 1986

Senator CRANSTON. Thank you very much, Ira.

Now we go to Mr. Lyle Gramley, chief economist and senior staff vice president, Mortgage Bankers Association of America. Mr. Gramley.

STATEMENT OF LYLE GRAMLEY, CHIEF ECONOMIST AND SENIOR STAFF VICE PRESIDENT OF THE MORTGAGE BANKERS ASSOCIATION OF AMERICA

Mr. GRAMLEY. Thank you, Mr. Chairman.

As other witnesses have testified this morning, the proportion of households owning their own home has been declining since 1980, and this decline has been concentrated among younger households.

Among households headed by persons less than 35 years of age, homeownership rates have declined quite dramatically, and it is from these age groups that most first-time home buyers come.

The principal explanation of declining homeownership in recent years is the high cost of homeownership. The problem is one of affordability.

The most well-known index of housing affordability is published by the National Association of Realtors and is shown in exhibit 6 that was attached to my prepared statement.

This index focuses on the principal cash costs faced by a home buyer, the monthly payment of interest and principal.

The NAR index indicates that housing affordability in the first quarter of 1987 was at levels not seen in almost a decade. But it also indicates that housing is considerably less affordable today than it was during the early years of the 1970's.

Exhibit 7 in my testimony seeks to identify some of the underlying reasons for changes in the affordability of housing since 1970. The 1970's were years of high inflation which led to a dramatic increase in mortgage interest rates and home prices rose sharply as well.

From 1970 to 1981, the cash cost of housing increased much faster than family income. Since 1981, inflation has come down, mortgage interest rates have fallen and home prices have risen more slowly.

The cash cost of housing has actually declined since 1981. Changes in the rate of inflation, I believe, are the principal source of changes in the cash cost of homeownership and in this measure of affordability.

My prepared statement discusses more comprehensive measures of housing costs and affordability that take into account future appreciation in the value of homes.

To younger individuals and first-time home buyers, however, the cash costs of homeownership are likely to be the most critical. An increase in the cash cost may prohibit such an individual from buying a house, even though appreciation in its value might make it an attractive investment.

Measures of cash affordability for families classified by age of family head, which are shown in exhibit 10 submitted with my testimony, indicate dramatic declines in cash affordability for younger families.

Between 1970 and 1986, cash affordability declined by nearly a half for families in the 15–24 age group, a third for those in the 25–34 age group and about a fourth for older families.

For younger families, too, another important obstacle to homeownership is the size of the down payment. Exhibit 11 shows what a 10 percent down payment on an average-priced home amounts to as a percent of median family income by age of family head.

For families in the 15–24 age group, the figure rose from 41 percent in 1970 to 62 percent in 1986. For those in the 25–34 age group, the increase was from 29 to 35 percent.

Exhibit 11, I think, makes a very important point. If the FHA and VA programs with their low down payment requirements were needed in 1970 to help younger families purchase a home, and they were, they are needed even more today.

Let me turn now to policies to make housing more affordable, especially for those segments of the population for which homeownership rates have been declining in recent years.

First and foremost, our nation needs to keep inflation under control. While that is partly the province of monetary policy, other governmental policies affect inflation as well.

We cannot realistically expect to bring down inflation further unless the Federal budget deficit continues to decline. Equally important, I believe, is the avoidance of protectionist measures, which would harm our economy in a variety of ways, including potentially damaging effects on inflation and on the affordability of housing.

Second, a concerted effort needs to be made to bring down real interest rates, which are still quite high by historical standards. Reductions in the Federal budget deficit are the most promising way to accomplish that objective.

Beyond these broad measures there are other cost-effective steps that the Federal Government can take to improve the affordability of housing. Chief among these is to maintain the viability of the FHA, VA, Ginnie Mae, Fannie Mae, and Freddie Mac programs.

My prepared statement includes a list of specific initiatives supported by the MBA relating to those programs.

That completes my oral statement, Mr. Chairman.

[The complete prepared statement of Lyle E. Gramley follows:]

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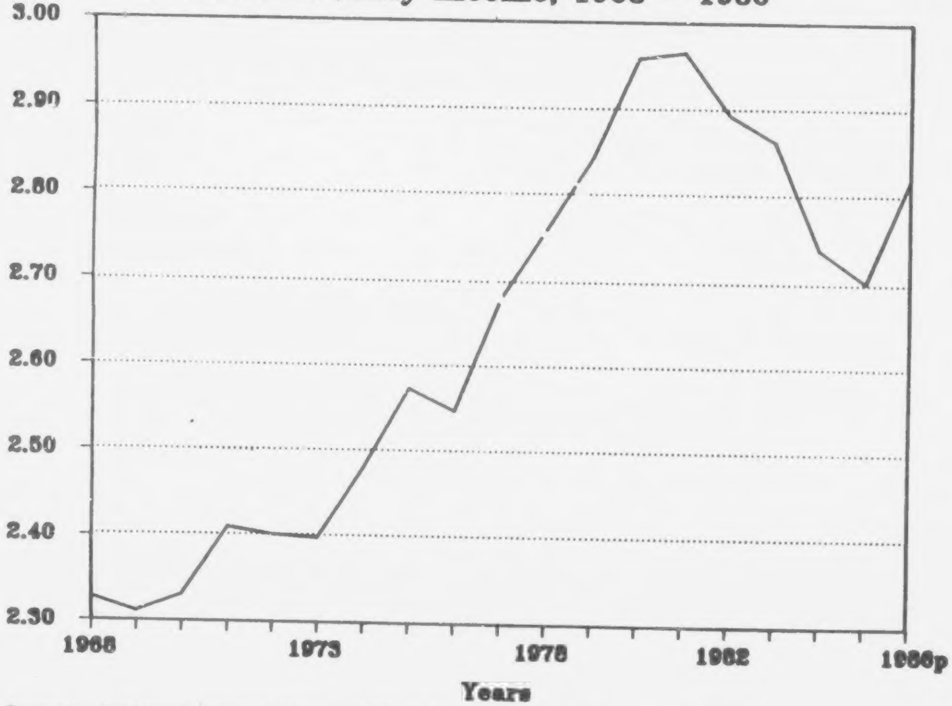
Exhibit 4

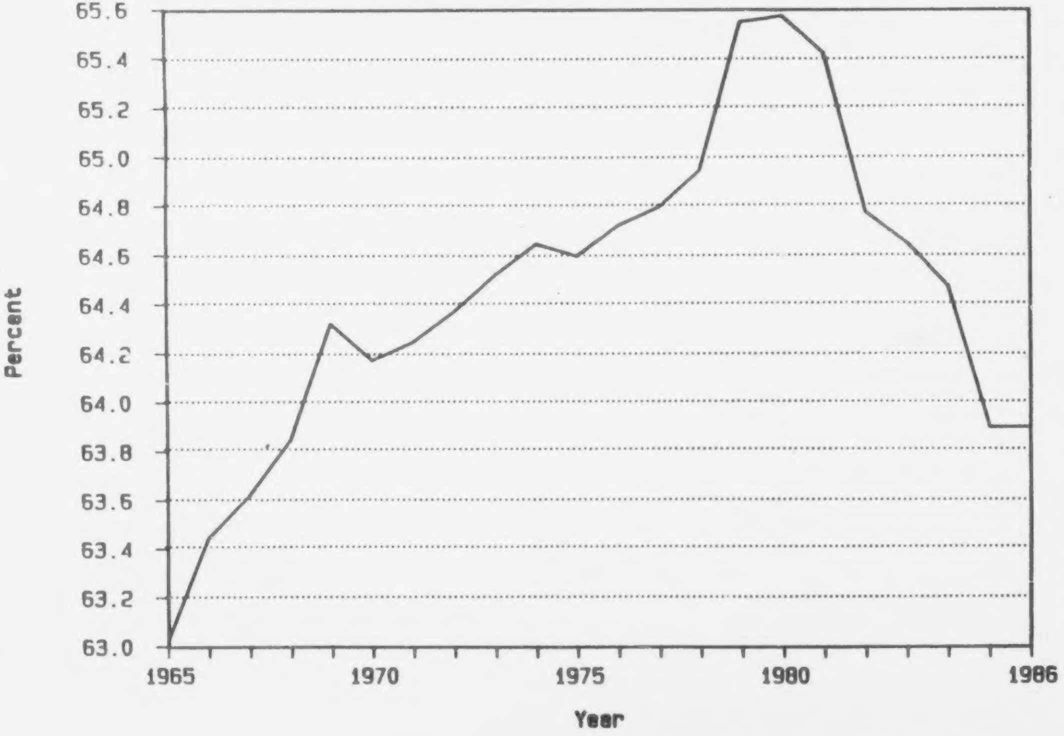
Ratio, Existing Single-Family Median Home Prices to Median Family Income, 1968 - 1986



Source: National Association of REALTORS; U.S. Bureau of the Census

Exhibit 5

Homeownership Rate, 1965 to 1986



Source: U.S. Bureau of the Census

1125 Fifteenth Street, N.W.
Washington, D.C. 20005
202-861-6500

Mortgage Bankers Association of America

STATEMENT OF

LYLE E. GRAMLEY
SENIOR STAFF VICE PRESIDENT
AND CHIEF ECONOMIST

on behalf
of the

MORTGAGE BANKERS ASSOCIATION OF AMERICA

before the

COMMITTEE ON BANKING, HOUSING AND URBAN AFFAIRS
SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS

UNITED STATES SENATE

Hearings on

Affordability of Housing

July 1, 1987

Mr. Chairman and members of the Subcommittee, my name is Lyle E. Gramley. I am Senior Staff Vice President and Chief Economist of the Mortgage Bankers Association of America (MBA).* Accompanying me today are Brian D. Cooney, MBA Associate Legislative Counsel, and Richard W. Peach, MBA Senior Director.

MBA appreciates the opportunity to appear before you today to testify on the affordability of homeownership.

Nearly 40 years have passed since the Federal government established a national housing policy by passing the Housing Act of 1949. That Act set forth as our nation's goal "a decent home and a suitable living environment for every American family." Homeownership has become symbolic of the achievement of that objective. As President Reagan stated in the 1982 Report of the President's Commission on Housing, "Owning one's own home . . . is a concept deeply rooted in the hearts of our people, for it carries with it a constellation of values—family, neighborhood, community independence, self-reliance, faith in our country and its future."

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*The Mortgage Bankers Association of America is a nationwide organization devoted exclusively to the field of housing and other real estate finance. MBA's membership comprises mortgage originators and servicers, as well as investors, and a wide variety of mortgage industry-related firms. Mortgage banking firms, which make up the largest portion of the total membership, engage directly in originating, selling, and servicing real estate investment portfolios. Members of MBA include:

- Mortgage Banking Companies
- Commercial Banks
- Mutual Savings Banks
- Savings and Loan Associations
- Mortgage Insurance Companies
- Life Insurance Companies
- Mortgage Brokers
- Title Companies
- State Housing Agencies
- Investment Bankers
- Real Estate Investment Trusts

MBA headquarters is located at 1125 15th Street, N.W., Washington, D.C. 20005; telephone: (202) 861-6500.

As the Subcommittee is well aware, the proportion of households owning their own home—the homeownership rate—grew steadily during the first three decades after World War II, to 65.6 percent in 1980 (Exhibit 1). A strong economy, relatively low mortgage interest rates, and a strong Federal government commitment to improve the quantity and quality of housing were all contributing factors to this increase. Since 1980, the homeownership rate has fallen steadily, to 63.8 percent in 1986. Had the homeownership rate remained at the 1980 level, there would be approximately 1½ million more households today owning their own home. Changes in preferred living styles and arrangements may be partly responsible for this decline in homeownership, but the available evidence indicates that reduced housing affordability, particularly for households headed by younger persons, is mainly responsible.

Not surprisingly, during this recent period of declining homeownership rates, the proportion of our Gross National Product devoted to residential investment has been comparatively low (Exhibit 2). During the 1950s, 1960s, and 1970s, residential investment comprised approximately 5¼ percent to 5½ percent of real GNP. In only one of the past seven years, 1986, was the ratio over 5 percent.

The decline in homeownership since 1980 has not been spread evenly among the various age groups; it has been concentrated among younger households (Exhibit 3). Among households headed by persons 50 years or older, the rate of homeownership has been essentially unchanged over the past six years. In contrast, among households headed by persons less than 35 years of age, homeownership rates have declined quite dramatically, and it is from these age groups that most first-time homebuyers come. Thus, the dream of owning one's home has become increasingly unattainable for a substantial segment of the population.

One reason for the concentration of declining homeownership among younger households is their relatively unfavorable income experience (Exhibit 4). Since 1970, annual rates of change in median family income have been considerably higher for families headed by older persons than for younger families. This has been particularly evident during recent years. From 1980 to 1986, annual rates of change in median family income ranged from a little below 2 percent for families in the 15-to-24 age group to about 8 percent for families in the 65-and-over age group. From 1970 to 1986, the annual rate of change in consumer prices was 6 3/4 percent. Families headed by persons less than 34 years of age have thus experienced declines in real family income.

By geographical area (Exhibit 5), homeownership rates have declined since 1980 in all of the four major regions of the country except the Northeast. Homeownership rates in the Northeast have been sustained at close to 1980 levels by very rapid growth of the regional economic base—despite rather large increases in new and existing home prices, especially in the past few years.

While differences in growth rates of real income help to explain divergences in homeownership rates among age groups and regions of the country, the principal explanation of declining homeownership in recent years is the high cost of purchasing a home.

MEASURING AFFORDABILITY

Homeownership cost may be measured in alternative ways—before or after taxes, focusing just on the monthly payment of interest and principal or including other homeowner costs, measuring out-of-pocket expenses only or including other costs as well. None of the available indexes of housing affordability deals with the various elements of homeowners' costs in a fully satisfactory fashion. But they all indicate that housing is less affordable now than in most postwar years prior to 1977.

The most well-known index of housing affordability is published by the National Association of Realtors (NAR). This index focuses on the principal cash costs faced by a homebuyer--the monthly payment of interest and principal. Other cash costs such as property taxes, utilities, insurance, and maintenance and repairs are not explicitly included. Moreover, the interest cost is treated on a pre-tax basis. While these simplifying assumptions are a limitation in using the index to measure affordability, it is widely recognized that variations in mortgage interest rates and home prices are the principal sources of change in the cash costs of homeownership.

In the NAR index, monthly payments of interest and principal are estimated based on prevailing mortgage interest rates, the median price of existing single-family homes sold, and an assumed 20 percent downpayment. The amount of income necessary to qualify for such a loan is calculated based on underwriting guidelines established by the Federal National Mortgage Association (FNMA) and the Federal Home Loan Mortgage Corporation (FHLMC). The magnitude of income needed to qualify for a loan relative to median family income determines the affordability of a home.

The NAR index, shown in Exhibit 6, indicates that housing affordability in the first quarter of 1987 regained levels not seen in almost a decade. The NAR index also indicates that, from a cash cost standpoint, housing is considerably less affordable today than it was during the early 1970s.

Exhibit 7 seeks to identify some of the underlying reasons for the deterioration in the affordability of housing in the 1970s, and the more recent improvement, reflected in the

NAR index. Shown there are annual rates of change in median family income and the monthly principal and interest (P&I) payment from 1970 to 1981, and from 1981 to 1986, along with annual rates of change in consumer prices and wages over the same two periods.

The message in these statistics is a rather simple one. The 1970s were years of high inflation. Real incomes showed little increase, because productivity growth was low and rising prices of foreign oil were draining income from the United States. Inflation led to a dramatic increase in mortgage interest rates, and home prices rose sharply as well. The cash costs of housing increased much faster than family income. Since 1981, inflation has come down, mortgage interest rates have fallen, and home prices have risen more slowly. The cash costs of housing have actually declined, while median family income has advanced at a pace somewhat above the rate of inflation. Changes in the rate of inflation are clearly the principal source of changes in the cash cost of homeownership and in this measure of affordability.

Members of the Subcommittee will recognize that the cash costs of housing fail to take account of the fact that homeowners enjoy the benefit of appreciation in the value of their home. More comprehensive measures of housing costs and affordability seek to measure that implicit element of costs (or benefits).

Exhibit 8, for example, shows estimates by the Harvard/MIT Joint Center for Housing Studies of the relation between cash costs and total costs of homeownership, each shown as a percentage of median household income. During the 1970s, rates of home price appreciation were high compared with the level of mortgage interest rates. During those years, the total costs of homeownership were low relative to cash costs. More recently, rates of home price appreciation have been low relative to the level of mortgage interest rates, so that the total cost of homeownership has risen sharply relative to the cash cost. In 1986, total costs of homeownership as a percent of median income were much higher, relative to the years of the 1970s, than was the case for cash costs.

This difference between cash costs and total costs of homeownership corresponds roughly to the difference between nominal and real mortgage interest rates (Exhibit 9). From 1970 through 1978, increasing nominal mortgage interest rates were accompanied by an even faster rise of home prices. Consequently, real mortgage interest rates declined and were negative from the mid-1970s until 1981. Real mortgage interest rates rose to dramatic heights during the first half of the 1980s before turning down. Today's level of real mortgage interest rates is still very high by historical standards.

The two measures of cost are both important because they have relevance for potential homebuyers in different financial situations. To an individual whose annual income is barely enough to meet the qualifying income of a typical mortgage lender, the cash cost of homeownership is likely to be more critical. An increase in the cash cost may prohibit such an individual from buying a house, even though future appreciation in the value of that house might make it an attractive investment. Many younger individuals contemplating purchase of their first home fall into this category. For a person whose current income is well above qualifying levels, the total cost of homeownership may be the more relevant measure. High total costs of homeownership may encourage such an individual to meet his or her needs for shelter by renting rather than purchasing, or by acquiring a smaller home. Older heads of households, second-time homebuyers, and individuals in higher income brackets fall into this category.

Both concepts of costs and affordability help to explain why homeownership rates have declined in recent years. High cash costs early in the 1980s kept many younger, first-time

homebuyers out of the market for several years. At the same time, the continued relatively high levels of real mortgage interest rates and total homeownership costs help to explain why single-family housing starts and sales in the past two years have remained below the levels of the late 1970s, when nominal mortgage interest rates were close to those prevailing today.

The fact that homeownership rates have declined most among younger heads of households suggests that high cash costs of homeownership are the principal reason why rates of homeownership have been falling. Measures of affordability for families classified by age of family head illustrate this point.

Exhibit 10 shows indexes of cash affordability by age of family head. These indexes are constructed by dividing median family income of each age group by the NAR measure of qualifying income. The central message is told by the figures at the bottom of the table. Between 1970 and 1986, cash affordability declined by nearly one half for families in the 15-to-24 age group, one third for those in the 25-to-34 age group, and about one fourth for older families.

For younger families, families in lower-income brackets, and first-time homebuyers, high cash costs are not the only obstacle to homeownership. Often, the principal hurdle that must be surmounted is the size of the downpayment. To illustrate this point, Exhibit 11 shows what a 10 percent downpayment on an average-priced home amounts to as a percent of median family income by age of family head. For families in the 15-to-24 age group, the figure rose from 41 percent in 1970 to 62 percent in 1986; for those in the 25-to-34 age group, the increase was from 29 to 35 percent. For older age groups, the increase was smaller, and it actually declined for families in the 65-and-over age bracket.

Exhibit 11 makes a point that I would like to emphasize. If the FHA and VA programs, with their low downpayment requirements, were needed in 1970 to help younger families realize their dream of owning their own home, they are needed even more today. That is the reason why the Mortgage Bankers Association has fought so hard to keep the Administration from gutting those programs.

POLICY RECOMMENDATIONS

Let me turn now to what needs to be done to make housing more affordable, especially for those segments of the population for which homeownership rates have been declining in recent years.

First and foremost, our nation needs to avoid a resurgence of inflation that would raise interest rates, increase the price of homes, and reduce housing affordability. The underlying or core inflation rate (the rate of inflation excluding food and energy) is now in the range of 4 percent, well below the rates prevailing in the late 1970s and 1980s. During the course of the current economic expansion, which is now in its fifth year, the underlying inflation rate has not increased, and that is certainly a noteworthy accomplishment. But there is no reason to be satisfied with 4 percent inflation. We can, and should, aim to do better. A further reduction of inflation would be most beneficial for younger households and first-time homebuyers, because it would reduce the cash costs of homeownership, which are particularly critical for this segment of the population.

Controlling inflation is partly the province of monetary policy, but other governmental policies can affect inflation as well. Federal budgetary policy is one of them. We cannot realistically expect to bring down inflation further unless the Federal budget deficit

continues to decline. Progress in reducing the deficit in fiscal 1987 is quite heartening, but there is still a long way to go to bring Federal outlays and revenues into reasonable balance. Equally important in the outlook for inflation, I believe, is the avoidance of protectionist measures. The protectionist sentiment sweeping our country is deeply disturbing. Protectionist measures will harm our economy in a variety of ways, including potentially damaging effects on inflation and on the affordability of housing.

Second, a concerted effort needs to be made to bring down real interest rates, which are still quite high by historical standards. Perhaps we can never return to the very low real interest levels of the early 1970s or the earlier years of the postwar period. During those years, there were substantial blockages of credit flows to various segments of the economy because of usury laws, ceilings on the rates that depository institutions could pay to attract deposits, and other factors. Removing those barriers to credit flows has made money and capital markets function more efficiently, and has opened access to credit to individuals and businesses that would otherwise be unable to borrow. The consequence, however, is that real interest rates now do the lion's share of the rationing of available funds among potential borrowers. They are therefore higher than they would be in a world in which a substantial amount of nonprice credit rationing occurred. Nonetheless, even under present circumstances, real interest rates would be lower if the Federal government reduced its demands on the credit markets.

Reduction in the Federal deficit is thus a key ingredient in bringing down both real and nominal interest rates, and through that route in making housing more affordable. MBA strongly supports measures to bring down the Federal deficit. MBA believes that no area of Federal outlays, including defense spending, should be immune from scrutiny. MBA would also support broad-based tax increases, should they be necessary, to close the gap between Federal outlays and revenues.

Beyond these broad measures, there are other cost-effective steps that the Federal government can take to maintain and improve the affordability of housing. Chief among these is maintaining the viability of the FHA, VA, Government National Mortgage Association (GNMA), FNMA, and FHLMC programs that are critical to continuing the opportunities for middle-income American families, and especially first-time homebuyers, to buy a home. These housing credit agencies are a prime example of government implementation of economic and social policy in a cost-effective way, while at the same time allowing for maximum involvement of the private sector in achieving the goals of housing policy. They have played an instrumental role in the development of a secondary market for mortgages, thus adding to the available supply of mortgage credit and holding down its cost.

MBA strongly supports the following specific initiatives that would help to maintain and increase homeownership affordability:

— Prohibiting new or increased user fees for FHA, VA, GNMA, FNMA, or FHLMC.

— Granting the FHA single-family mortgage insurance program permanent insuring authority.

— Retaining the ability of borrowers to finance closing costs in FHA loans.

— Increasing the FHA high-cost area maximum insurable mortgage amounts for single-family and multifamily residences.

— Providing adequate credit budget authority for the FHA and GNMA programs.

— Removing the volume limitation for FHA-ARMs.

— Reinstituting the full deductibility in the year the transaction is consummated of points paid in connection with a mortgage refinancing.

— Prohibiting the imposition of an aggregate limit on the volume of mortgages FHLMC or FNMA can purchase.

— Increasing the maximum VA guaranty to $36,000, as provided for in the Senate VA bill.

— Authorizing VA to guaranty ARMs.

— Exempting the VA guaranty authority from sequestration under Gramm-Rudman-Hollings budget law.

MBA appreciates the opportunity to testify before this Subcommittee and would be happy to answer questions or provide additional information, as necessary, for inclusion in the record.

Exhibit 1

Homeownership Rate

(Percentage of Households Owning Their Home)

1940	43.6
1950	55.0
1960	63.1
1970	64.2
1975	64.6
1980	65.6
1981	65.4
1982	64.8
1983	64.6
1984	64.5
1985	63.9
1986	63.8

Source: Department of Commerce, Bureau of the Census

Exhibit 2

Residential Investment as a Percentage of GNP

(1982 Dollars)

1950s	5.66
1960s	5.24
1970s	5.34
1980	4.30
1981	3.89
1982	3.32
1983	4.55
1984	4.89
1985	4.94
1986	5.28

Source: Department of Commerce, Bureau of Economic Analysis

Exhibit 3

Homeownership Rate by Age of Head of Household

Age of Household Head	1981	1982	1983	1984	1985	1986	Percent Change 1981-1986
Under 25	20.7	19.3	18.8	17.9	17.2	17.2	-16.9
25-29	41.7	38.6	38.3	38.6	37.7	36.7	-12.0
30-34	59.3	57.1	55.4	54.8	54.0	53.6	-9.6
35-39	68.9	67.6	66.5	66.1	65.4	64.8	-6.0
40-44	73.7	73.0	72.8	72.3	71.4	70.5	-4.3
45-49	76.2	76.0	75.2	74.6	74.3	74.1	-2.8
50-54	78.3	78.8	78.8	78.4	77.5	78.1	-0.3
55-59	80.0	80.0	80.1	80.1	79.2	80.0	0.0
60-64	80.0	80.1	79.7	79.9	79.9	79.8	-0.2
65 and over	73.9	74.4	75.0	75.1	74.8	75.0	1.5
All Households	65.4	64.8	64.6	64.5	63.9	63.8	-2.4

Exhibit 4

Annual Rates of Change in Median Family Income, by Age of Family Head (Percent)

Age of Family Head:	1970-75	1975-80	1980-86	1970-86
15-24	4.4	9.5	1.8	4.9
25-34	6.7	8.4	4.9	6.4
35-44	6.9	9.2	5.8	7.2
45-54	7.7	9.2	6.1	7.6
55-64	7.4	9.6	5.4	7.3
65 and over	9.8	9.8	7.9	9.1
Memo: Percentage Change in Consumer Prices, Annual Rate.	6.7	8.9	4.9	6.7

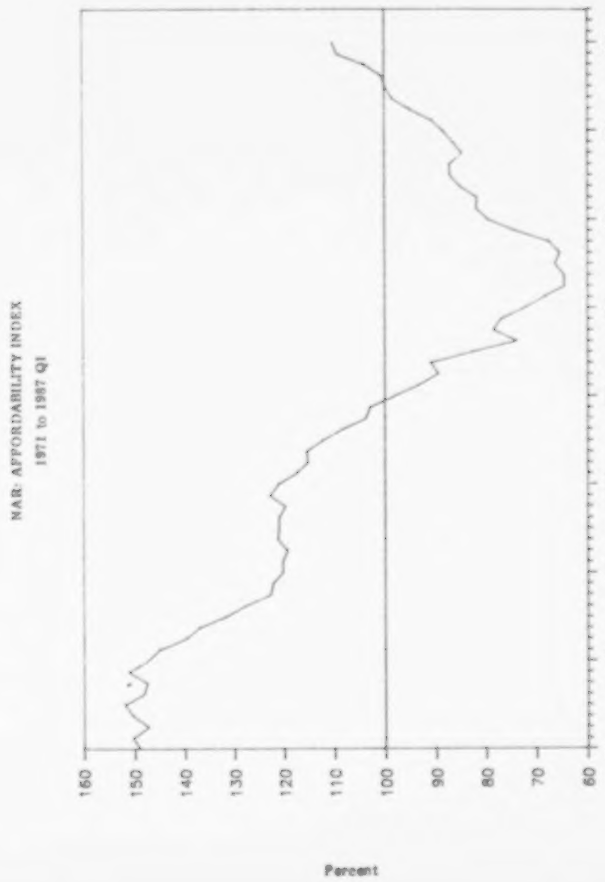
Exhibit 5

Homeownership Rates by Region

	Northeast	Midwest	South	West
1980	60.8	69.8	68.7	60.0
1981	60.8	69.7	68.2	60.2
1982	61.1	69.4	66.7	59.4
1983	61.5	69.3	67.0	58.2
1984	61.2	68.4	67.0	58.5
1985	60.8	66.9	66.4	59.0
1986	61.4	66.9	66.1	58.3

Source: Department of Commerce, Bureau of the Census

Exhibit 6



Source: National Association of Realtors

Exhibit 7

Percent Change, Annual Rate

	1970-81	1981-86
Median Family Income	7.7	5.0
Monthly Payment of Interest and Principal	15.4	-3.2
Home Price	10.1	3.9
Mortgage Rate	5.5	-7.5
Consumer Prices	8.0	3.8
Average Gross Hourly Earnings [1]	7.4	3.8
Average Gross Weekly Earnings [1]	7.1	3.6

[1] Private Nonfarm Economy

Exhibit 8

Housing Costs as a Percentage of Median Household Income (Recent Purchasers)

	Total Costs [a]	After-tax Cash Costs [b]
1970	11.6	21.9
1971	15.4	22.9
1972	7.0	23.5
1973	11.0	26.6
1974	11.0	28.5
1975	13.0	29.9
1976	9.2	30.7
1977	8.1	31.4
1978	7.1	34.8
1979	10.6	35.7
1980	24.0	36.9
1981	35.5	35.7
1982	41.6	37.4
1983	32.2	31.8
1984	33.7	32.0
1985	30.2	31.6
1986	27.8	30.4

[a] Total costs equal after-tax cash costs plus the opportunity cost of the homeowners equity minus the expected annual appreciation of the home.

[b] After-tax cash costs equal the sum of after-tax mortgage payments, after-tax property tax payments, expenses for utilities, maintenance and repairs, and insurance and transaction costs.

Source: 1970 to 1985, Harvard/MIT Joint Center for Housing Studies; 1986, estimate by MBA.

Exhibit 10

Indexes of Cash Affordability By Age of Family Head

	15 - 24	25 - 34	35 - 44	45 - 54	55 - 64	65 and Over
1970	105.1	147.2	170.4	181.0	155.1	147.4
1971	102.0	151.6	175.4	190.4	162.2	151.8
1972	103.6	155.3	182.5	195.6	162.5	154.7
1973	98.3	149.7	175.4	186.7	156.7	147.8
1974	87.3	130.7	154.9	167.2	137.5	130.3
1975	78.8	122.9	143.2	158.1	133.8	123.4
1976	79.4	124.4	146.2	160.1	135.5	125.8
1977	78.1	119.2	142.0	156.9	129.7	120.6
1978	75.3	109.7	129.3	142.8	122.0	111.3
1979	64.3	95.6	113.4	125.3	108.6	97.2
1980	52.4	77.5	93.7	103.5	89.4	79.8
1981	43.1	66.2	81.5	90.0	77.5	68.9
1982	42.3	66.1	81.5	91.1	77.4	69.5
1983	46.9	77.1	98.0	110.3	92.8	83.2
1984	46.5	84.8	105.1	116.3	98.8	89.1
1985	51.6	89.0	111.7	125.4	104.7	94.8
1986	55.6	99.1	125.2	140.7	116.8	106.2
Percent Change 1970 to 1986	-47.1	-32.7	-26.5	-22.3	-25.7	-28.0

Source: Department of Commerce, Bureau of the Census; National Association of Realtors; and Mortgage Bankers Association of America. Indexes are computed by dividing median family income by the NAR measure of qualifying income.

Exhibit 11

Ten Percent Downpayment as a Percentage of Median Family Income[a]

	1970	1975	1980	1986
Age of Family Head:				
15-24	41	49	54	62
25-34	29	31	36	35
35-44	25	27	30	28
45-54	24	24	27	25
55-64	28	29	32	30
65 and over	57	53	58	47
All Families	29	31	35	32

Source: Department of Commerce, Bureau of the Census; Mortgage Bankers Association of America

[a] Downpayment is calculated as 10 percent of the price of a constant quality new home as estimated by the U.S. Department of Commerce, Bureau of the Census.

Senator CRANSTON. Thank you very, very much.

The final member of the panel is Mr. Earl Corkett, president, Mortgage Insurance Companies of America.

We welcome you.

STATEMENT OF EARL CORKETT, PRESIDENT, MORTGAGE INSURANCE COMPANIES OF AMERICA

Mr. CORKETT. Thank you, Mr. Chairman.

I am Earl Corkett, chairman of PMI Mortgage Insurance Company, headquartered in San Francisco, CA. I also serve as president of Mortgage Insurance Companies of America, MICA, the trade association representing all the private mortgage insurance companies in this country.

I am a businessman representing companies whose primary purpose is to expand homeownership opportunities. Currently, we assist over 3 million home buyers.

Our formal statement has been submitted, and I would like to highlight several points on the affordability issue at this time.

The opportunity to own a home must continue into the future as a cornerstone among our democratic principles, and it deserves a high priority by the Congress among the array of choices for the allocation of Government resources.

Our housing policy must reflect changes that occur in the housing finance system, and there have been plenty of changes recently that affect affordability.

Because of the budget deficits, the controlling of Government spending will be essential to this Nation's economic strength and to the cost of long-term credit, including mortgage credit. The cost of mortgage credit is a key element in housing cost.

Budget deficits cannot be reduced unless the following democratic principle is recognized:

Those who have the means to pay market rates and obtain affordable housing through the conventional market without the assistance of Government should be encouraged to do so. Government-supported incentives should be targeted and must not harm the operation of competitive markets.

There have been many developments in the marketplace that provide lessons on affordability, not the least of which is the problem of foreclosure. Foreclosures represent families who have lost their homes, families who have met with a personal home affordability crisis.

We can develop all the macro statistics on disposable income, median home prices, affordability indexes, et cetera, but when you really get down to it, in order to have an understanding of affordability we have got to look at the effects on the individual home buyer.

In this regard mortgage insurers have a unique industry perspective on affordability, since our profitability is directly determined not only by how well we help borrowers afford a home purchase but how correct we are in assessing if the home transaction will allow the borrower to stay in his home.

Fortunately, today many more real estate professionals have recognized that the definition of affordability must go beyond the initial purchase and include the many costs of maintaining the home.

By not fully recognizing this definition and by not responding more quickly than we did to such factors as negative amortization, buydowns, sales concessions, and many, many other financing techniques that were introduced into housing markets, mortgage insurers paid dearly. The incurred losses for this industry set another record in 1986, reaching about $1.2 billion.

While claims provide lenders and investors substantial financial benefits, each claim represents the financial distress of an American family. They also paid dearly.

We have learned the lessons about affordability of home financing arrangements and because of the significant increase in mortgage credit risk, the industry developed more realistic guides for underwriting home buyers.

I must note here in this regard that some groups criticize the new tighter underwriting requirements supposedly on behalf of the home buyer, claiming that changes would eliminate the opportunity for many to afford a home. After the foreclosure experience in certain markets in the early 1980's, we have now learned that the volume of homes sold or loans closed is not necessarily an indicator of affordability.

It is the nature of private firms to adjust to change. If they don't, they perish. The Government can be less responsive, and this can create problems, also.

For example, the evidence shows that during the time private insurers began to tighten underwriting policies mortgage lenders responded by simply shifting to the more liberal FHA programs, and in this case created an oversupply of housing in certain regional markets.

A lot has been said about the volume of FHA. We would urge the subcommittee over the next several months to look at recent FHA loans, which borrowers by income got loans, how many loans for new construction or for refinance, and in what price range, and what is the loss experience.

The FHA 203(b) program has not had an underwriting profit since 1983 and has in recent months reportedly been receiving record numbers of properties in insurance claims from lenders.

When the FHA overstimulates a market by creating false affordability, it doesn't help home buyers.

MICA has consistently said FHA can play an important role in expanding homeownership affordability, but if FHA is failing to target the lower income and the first-time home buyers, most in need of assistance to afford a home, the new policy for that program is warranted.

To that end we are commissioning an independent study of the insured home loan markets served by both FHA and private industry. We believe this study will provide significant information which will aid this subcommittee and others who will be studying housing policy issues later this year. We expect this study to be available early this fall.

In summary, we recommend the following:

Define affordability to include the continuum of the entire payment period.

Target scarce Government resources to do the most for lower income families and encourage private enterprise to expand their role in meeting the housing needs of American families.

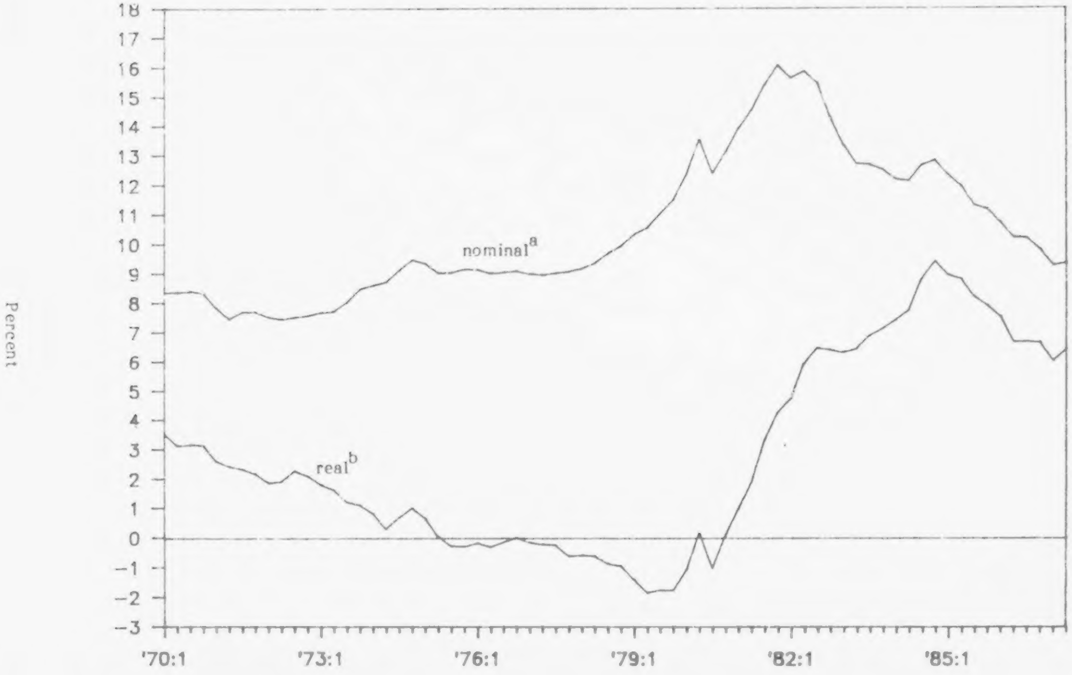
Private mortgage insurers stand ready to expand our role in providing housing affordability.

We are pleased to be here today, and we look forward to meeting your questions.

[The complete prepared statement of C. Earl Corkett follows:]

NOMINAL AND REAL MORTGAGE RATES

1970 to 1987 Q2



a - Effective Mortgage Rate on Conventional Loans Closed, Source: Federal Home Loan Bank Board

b - Nominal Mortgage Rate Less 3-Year Moving Average of Average Constant Quality Home Price, Source: Mortgage Bankers Association of America

Note: Average Constant Quality New Home Price obtained from the Bureau of the Census.

Exhibit 9

STATEMENT OF C. EARL CORKETT, PRESIDENT OF THE MORTGAGE INSURANCE COMPANIES OF AMERICA. BEFORE THE SENATE HOUSING SUBCOMMITTEE ON THE ISSUE OF HOUSING AFFORDABILITY.

Wednesday, July 1, 1987

Mr. Chairman and Members of the Subcommittee:

I am Earl Corkett, the Chairman of PMI Mortgage Insurance Company located in San Francisco, California. I serve as the President of the Mortgage Insurance Companies of America (MICA),* the trade association representing all the private mortgage insurance companies.

It is a welcome opportunity for me to present MICA's views as part of this oversight hearing. We sincerely believe that the issue of housing affordability lies at the heart of housing policy and we believe this hearing is an excellent preface for later hearings in which the Subcommittee will seek to update the appropriate direction that our nation's housing policy should take.

Defining Home Affordability

The Subcommittee has requested an assessment of housing affordability from the industry perspective. The individual industries represented on this panel constitute different sectors of the housing industry and therefore bring different perspectives to the problems of housing affordability. All the groups including MICA are concerned with the recent trend toward high relative housing costs. The levels of median home prices have continued to rise and there are higher costs each year for utilities, maintenance and taxes. These rising costs are even more significant when combined with the lower rate in increases of disposable income.

While private mortgage insurance companies have common concerns with the other housing groups, our perspective is unique from other groups on this panel. The role of our insurance coverage in housing finance has been to substitute for borrowers equity allowing borrowers to obtain mortgages with low downpayments. Our concern is for the risk of default before the loan is repaid. Thus, when mortgage insurers look at affordability, they not only have a profit motive to get the buyer into an affordable home but to ensure that the home remains affordable for that borrower far into the future. We, therefore, urge this Subcommittee to recognize that a definition of affordability must go beyond initial purchase, and include the financing and other costs of maintaining the home as the years progress. Macro statistics are important for understanding affordability, but housing policy must be based upon the micro effects on affordability for the individual homeowner.

The business experience of private mortgage insurers is relevant to the issue of affordability because claims represent families who have lost their homes; families who have met with an affordability crises. The first half of the decade of the 1980's has been a difficult one for private insurers because of the large volume of claims. 1986 was this industry's worst year ever for

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*MICA consists of the thirteen domestic private mortgage insurance companies which represent the active firms that help loan originators and investors make funds available to homebuyers by protecting these institutions from a major portion of the risk of default. The current MICA officers are President, C. Earl Corkett of PMI, San Francisco; Vice President, William Lacy of MGIC, Milwaukee, WI; Treasurer, J. Edward Carlton of Integon Mortgage Guaranty Insurance Co., Winston Salem, NC; and Secretary, Fred Reichelt of Verex Assurance, Inc., Madison, WI. MICA also has private mortgage insurance companies members in Canada and Australia. At the end of 1986 the industry had over $267 billion of insurance in force.

losses. Incurred losses that are paid as benefits to mortgage bankers and other mortgage lenders were in the range of $1.2 billion. While the claims that have been paid to lenders and secondary market investors have provided very positive financial benefits, they also represent the financial distress of borrowers.

Our industry's recent claims experience holds some lessons for this issue of affordability. Mortgage insurers have found a number of factors which contributed to their losses. First, among these factors was the introduction of many new financing techniques such as adjustable rate mortgages, negative amortization and buydowns. Several forces spurred the development of these new financing techniques including the increased pressures on mortgage lenders to raise earnings due to deregulation. This forced many to become "volume oriented."

Mortgage insurers, themselves traditionally very competitive, did not immediately recognize the results this trend would bring. The industry had historically made its mark by "out-servicing" the FHA in competing for the loans of lenders and this competitive service orientation and our own desire for business made it easy for some private insurers not to recognize the greater risks that were then present in the residential market.

Now, however, we see how poorly some of the structured financing arrangements were for borrowers. We realize that affordable homeownership requires among other things, loan instruments and financing terms defined within a realistic set of parameters. In most markets, private insurers have made significant changes toward more realistic underwriting requirements. It should

be noted, however, that lenders, builders and realtors complained in published studies sent to members of Congress about the new underwriting posture that private insurers took. They complained on behalf of the homebuyer against our industry's tightening of underwriting requirements that was reducing the volume of homes being sold and loans being closed.

Again because of our role, our industry cannot be solely concerned with volume. Mortgage insurers continue to bear the risk of default for many years and, therefore, they must look at the financing from the perspective of the consumer. Will changes occur which decrease the value of the home or the affordability of financing? What will these changes do to the willingness of borrowers to repay? The claims of private insurers and the FHA's recent record volume of acquired properties contain evidence to show the importance of relating borrower equity to willingness to pay and ultimately to home affordability.

Another important lesson this industry has learned from its recent claims experience is that local housing markets can perform very differently from regional and national markets. Lenders, insurers, secondary market agencies and others must implement their programs to accurately reflect the relative risk of the local market. The homebuyer is not served by market stimulation that can result in a downturn of home values and or other destructive forces that can result when local market risks are hidden from the homebuyer.

An important illustration of this point was made by Dr. Barton Smith, Director of Center for Public Policy at the University of

Houston, before a meeting of key mortgage insurance executives when he described the way in which the Houston market was overstimulated in the early 1980's. He described that record home building continued in Houston long after the market was built to capacity. In the twelve months of 1982 the level of primary employment in Houston dropped by over 17 percent yet the home price index in Harris County where Houston is located increased by 18 percent. Consumers took advantage of favorable financing and lax underwriting standards that artificially expanded the affordability of homes. Homes should have been stable or decreasing rather than increasing in value. Many homebuyers eventually suffered hardships because normal market forces were impeded.

Mortgage insurers now recommend that housing policy recognize the need to keep consumers in their homes. The key to this recommendation is that all the players in housing finance must relate the risks in local markets to financing arrangements and underwriting requirements.

Government Role

In addition to examining the issue of affordability generally, we believe it is important that Congress conduct a detailed examination of the role government programs are playing in making home ownership affordable. Specifically, Congress must examine whether the FHA's recent role has expanded homeownership affordability or has simply shifted a large number of borrowers to the FHA program who typically could find affordable home financing in the conventional market. Congress must ask who should the government program serve in expanding affordability and what currently is the case. If the FHA program fails to target the lower income and first time borrower, typically viewed as those with higher credit risk and most in need of government assistance regarding affordability, then we believe new policy is warranted.

We also believe it is important that Congress examine whether government programs actually hinder the ability of the homeowner to afford his or her home once it is purchased by impeding the adjustment of market forces. How can the role of the government be controlled so that its programs achieve the goal of expanding realistic affordability of homeownership but does not overstimulate the market by absorbing an inappropriate level of risk?

There is now evidence from markets such as Houston, that when the private insurers began to make efforts to respond to higher risks, lenders simply shifted to the FHA government insurance. The FHA maintains a national underwriting policy and, therefore, was less responsive. As a result of the more liberal government underwriting the problem was exacerbated.

There are those industry groups that advocate national underwriting guides for FHA as being beneficial to homebuyers. These groups explain that FHA's comparative advantage over private insurers results from the ability of FHA to operate under one set of rules in all parts of the country. They cite recent statistics showing how many families were served by FHA when private insurers responded to market forces. While there is no question that FHA kept volume up, based upon the claim rates we are now seeing for FHA, not all homeowners were benefited. The FHA reported for a six

Senator **Cranston**. Thank you very, very much.

I have just a few questions, and again whoever chooses to answer, please do, and then if there is a comment, agreement or disagreement from other members of the panel, please express that.

Yesterday's Washington Post reported that new home sales plummeted 14.9 percent in May, the largest decline since January of 1982, when the Nation was in a recession.

What do you think accounted for that sharp decline in May? What does that tell us about what is happening in the housing industry, and what predictions do you have about short and long term developments there?

Mr. **Gramley**. I will be happy to start, Senator Cranston.

A dramatic increase in mortgage interest rates occurred from late March until the third week of May, and during a significant part of that period the mortgage market was in such turmoil that it was not functioning normally.

We had anticipated that housing would be adversely affected, but we didn't expect quite this large a decline in a single month. The rates of interest on mortgages have begun to come down since the third week of May. They are down 50 to 60 basis points. The market is now functioning normally.

I would anticipate that new home sales will recover somewhat, but I wouldn't expect them to get back to their first quarter levels.

Senator **Cranston**. Any other comments on that?

Mr. **Fischer**. Well, I will just say, Senator, that we, the home builders, still expect to have 1,600,000 starts this year.

Senator **Cranston**. Some of the witnesses today have testified that the affordability problem can partly be attributed to practices that the industry has introduced in recent times.

Mr. Hendrickson, for example, stated that:

> Although interest rates have declined significantly in the last 5 years, stricter credit underwriting standards have all but eliminated the benefits to first-time home buyers of the lower rates.

Are these statements correct? Has the industry undertaken or does it plan to undertake any initiatives to ease the difficulties faced by first-time home buyers?

Mr. **Corkett**. Mr. Chairman, I think there is a need here to once again focus on the definition of affordability to include the long-term holding period and ownership of that home. If someone is encouraged through a program that gets him into a home that he really can't afford, foreclosure results, and that is a worse disaster than if he didn't get into the home in the first place.

So let's be careful that we are talking about not just the entry into the home, but the ability to sustain that ownership.

Senator **Cranston**. Any other comments on that?

[No response.]

Senator **Cranston**. Mr. Fischer, I understand that you visited the Nehemiah Project on Monday of this week in New York. The housing bill now in conference would make Nehemiah type approaches available to other communities across the country.

I wonder what your reactions were to the project?

Mr. **Fischer**. Senator, I was very impressed in going through it. It is right in the heart of Brooklyn, and they have taken some old, old houses and torn them down and came up with some new plans and new houses, and it has really given the low income people a chance to have homeownership.

And the people we talked to—we interviewed some of the people around the yards that live there, and the pride that they have taken in their homes. They had roses all over their yards and some of them have put up metal gates and fences and really have taken pride in their homes, and you can see how a low income person can really enjoy having a home and homeownership when you go through and look at this Nehemiah Project.

I was very impressed with it, and I think it is good for a lot of places in our country.

Senator **Cranston**. Good. I am glad that was your reaction.

Mr. **Fischer**. I think it would revitalize a lot of towns that have old, old property and a lot of the cities that have lots on the market. They are not selling them. They have them back from tax defaults. And, this is something they could use to do good for their hometown.

Senator **Cranston**. I don't have any further questions. Has what has been said here led to any further thoughts that any of you would like to express about what we should do?

Mr. **Gribin**. I would like to say something about the point that Senator Chafee made. I think in order to solve the problem of housing you are going to need a partnership among five component parts.

I think you need a partnership among the Government because I think there is a lot of things that have to be done in zoning, in red tape, and things of that kind, and I think they become a critical factor in providing incentives.

I think the second thing that has to happen is the builder has got to get into the partnership. I think the kind of homes that they build are going to be absolutely critical to whether or not you are going to solve the problem of affordability because I think that to a great degree there is a tendency to build larger and larger homes rather than smaller and smaller.

I think the third group that has to get into the act are the unions. I think there has to be more technologically efficient ways to solve the problems of housing, and unless that is accomplished I think it is going to be difficult to solve the problem.

The fourth group I think are the lenders, who have simply preferred to make larger and larger loans to bigger and bigger homes because that is their job, to get money out into the marketplace.

And the last group, which may turn out to be the most difficult, are the homeowners themselves. Everyone wants progress down the street. No one wants progress in his or her neighborhood. Ultimately, we all will need to recognize the fact that homeownership is a basic, fundamental desire of every young person in this country and that there is going to be a serious problem in this area.

I think that a partnership among those five groups are absolutely critical to resolve this housing affordability problem.

Senator **Cranston**. Thank you, Ira.

Thanks to all of you very much. I appreciate all who testified and to all who were here. I appreciate your interest. Thank you very much.

We now stand adjourned.

[Whereupon, at 12:05 p.m., the subcommittee was adjourned.]

[Additional material supplied for the record follows:]

month period ending March 31, 1986 having received a record 23,798 properties in insurance claims from lenders.

Private insurers want to assist affordability for a large market of homebuyers as possible. At the same time that we desire to expand our role, the credit ratios and other ground rules for affordability must be economically sound. Private insurers do not have the capital to subsidize risk. Thus, they must identify borrowers and markets that are higher risk and react accordingly. However, the FHA can subsidize and help stabilize markets and MICA supports FHA being targeted to expand homeownership opportunities for those individuals who have less than moderate income and whose needs for government assistance are the greatest. We believe in a strong FHA program that is sensitive to local market conditions and avoids disruptive effects on the private market which will work to the detriment of many homebuyers.

On behalf of my association we sincerely appreciate this opportunity to participate at these hearings and look forward providing whatever help we can.

STATEMENT OF THE
COUNCIL OF STATE HOUSING AGENCIES

PREPARED FOR

THE HOUSING AND URBAN AFFAIRS SUBCOMMITTEE OF THE SENATE BANKING COMMITTEE

by

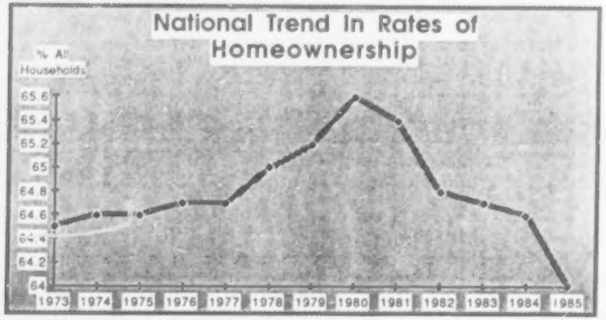
Carl W. Riedy, Jr.
Executive Vice-President

July 1, 1987

The Council of State Housing Agencies (CSHA) appreciates the opportunity to present a written statement before this Senate Housing and Urban Affairs Subcommittee. This hearing is an opportunity to begin a timely and fundamental debate on the issue of declining affordability and homeownership, which will have important implications for national housing policy. Since the Subcommittee will be hearing from a number of distinguished witnesses, including four representatives of state housing finance agencies (HFAs) from among our membership, CSHA's testimony will not dwell on the myriad examples of the affordability problem with which our members are contending. Instead, we will seek to present what CSHA regards as the key trends of recent years, what these trends mean for the nation, and their implications for the future.

Until the federal government made homeownership a central element of the national housing policies which were formulated during the Great Depression, a distinct minority of American families had the opportunity to purchase a home. We can now look back over nearly one-half century of continuing progress, both in expanding opportunities for homeownership--the means of access to this dream--and in the realization of that dream by ever increasing numbers of families.

Since 1980, the trend in homeownership has been one of erosion. The chart below, shows clearly just how the trend has emerged.



Source: U.S. Census Bureau

Today the homeownership rate is at its lowest level in a decade. No one single cause can be identified, the factors which have caused the abrupt change in the trend are multiple and complex. Prominent among the trends was the inflation which raged throughout the late seventies and into the 1980s driving interest rates to levels previously unimaginable. Yet even after the Federal Reserve squeezed inflation out of economy, real interest rates have remained high.

Throughout the period of inflation, incomes increased at rates lower than those of home prices. This defines the affordability problem, and is essential to an understanding of why it exists.

Inflation drove the cost of materials and labor ever higher over the course of a decade helping, in part, to create the gulf which exists and which has resulted in the trends in homeownership. Yet there are other factors that have been driving the cost of homes higher and continue to create pressure on home prices. In many areas of the nation, home sites are a commodity in limited supply. Land costs, coupled with the costs of subdivision improvements that are today typically borne by the developer, drive new home prices and indirectly impact upon the cost of exiting homes. In many areas of the country, the factor of site costs has driven home prices beyond the reach of increasing numbers of households.

Other factors apart from the influence of past inflationary periods are at work. Over the course of the past decade the housing finance system has changed. No longer is the five percent passbook savings the predominant source of capital for mortgages. Today mortgage capital comes predominantly from securities issued and traded in markets that are sensitive to investor demand. Mortgage interest is thus driven by the same factors which influence the broader financial markets, therefore reflecting some of the same volatility.

Lender requirements have also changed in recent years. Responding to increased defaults on high interest rate mortgages during the early 1980s, and in part to investor demand, underwriting criteria has been tightened. Coupled with these changes, not only has private mortgage insurance become more expensive, it is also increasingly out of the reach of more and more homebuyers. Naturally these changes have had the greatest impact upon the young, whose incomes are most limited. An Economic Policy Institute survey in 1983 found that 44 percent of a 30 year old homeowners income was spent for mortgage payment, compared with 21 percent a decade ago. For young working families with little potential growth in income, the prospects are daunting. In large part, this

is due to twin factors of recent origin: the higher entry cost of homeownership (down payment and closing costs), and, the carrying costs of homeownership (resulting from the combination of high prices and high interest costs).

The impact of the affordability problem on younger households is now quite clear. The following chart indicates the homeownership rate from 1981 to 1985 for various ages of the head of household.

Homeownership Rate According to Age of Householder

Age	1981	1982	1983	1984	1985
< 25	20.7	19.3	18.8	17.9	17.4
25-29	41.7	38.6	38.3	38.6	37.7
30-34	59.3	57.1	55.4	54.8	54.7
35-39	68.9	67.6	66.5	66.0	65.7
40-44	73.7	73.0	72.8	72.3	71.8
45-49	76.2	76.0	75.2	74.6	74.9
50-54	78.3	78.8	78.8	78.4	77.4
55-59	80.0	80.0	80.1	80.1	79.1
60-64	80.0	80.1	79.7	79.9	79.6
65-69	77.6	78.0	78.7	79.3	79.4
70-74	75.4	75.2	75.3	75.5	76.7
75>	69.8	71.0	71.9	71.5	70.4

Source: National Association of Homebuilders

Most troubling is the decline in homeownership among those households 35 years of age and under. The decline in homeownership was 15% for those under 25 in the past five years, and 8 percent for those aged 30-34. Americans have traditionally placed significant importance on owning one's own home: homeownership is seen as the culmination of the American Dream.

If today fewer Americans have the opportunity to enjoy the benefits of homeownership, we need to understand that the impact extends beyond these individuals. Had homeownership remained at 1980 levels, an additional 400,000 households would own their homes today. This equals perhaps 800,000 disillusioned Americans. The problems of these potential young homebuyers have to concern the 34 million parents with children under 18 who want their children to enjoy the American Dream.

Recently, mortgage markets boomed and housing starts were strong, bolstered by vigorous trade-up activity. Unfortunately, these trends did not represent the reality of the market for many. Even this vigorous trade-up market may be placed in jeopardy by the declining homeownership rate previously mentioned. These households are the potential trade-up buyers of the future. The economic consequences on the national housing finance system of this situation must be analyzed.

The current decline in homeownership has an impact on many sectors of the economy, the raw materials and construction materials providers, the builders, realtors, and lenders who are the "suppliers" of homes for the first-time homebuyer market, are all effected.

Expanding opportunities for homeownership has been one of the main goals of state housing finance agencies. Two primary tools have been Mortgage Revenue Bonds (MRBs) and the Mortgage Credit Certificate program (MCC). Over the last decade, the MRB programs of state HFAs have financed more than one million existing new homes, including more than 900,000 home purchases for first-time homebuyers. In 1985, while the average state MRB household income was $26,713, the national average income was $29,066. Moreover, MRB program participants paid an average of $54,343 for their homes in 1985, compared with a national average sales price of $99,500. The MRB homebuyer also paid an average downpayment of only 8%.

Tax Reform placed MRBs under the general tax-exempt bond volume cap imposed upon virtually all non-governmental tax-exempt securities. This drastically limits the remaining availability of this tool, which is set to sunset in December, 1988.

In addition to purchase price limits, which previously existed, income limitations were added as a new constraint. Even within these limits, a first time homebuyer market exists in most states, under current conditions. Exceptions are those urban and rural markets where a high housing cost/low income ratio exists. In addition, income limits, unlike purchase price constraints, are inelastic in volatile interest rate periods. As a result, in a high interest rate environment the statutory income limits will act as a formidable deterrent to utilizing MRBs as a countercyclical tool, as it was in 1981.

Lastly, in 1983, Congress created the Mortgage Credit Certificate for use by states as an alternative to the MRB. Twenty-one states converted some of their MRB allocation into MCCs in 1985, and many are finding that a market for these credits exists. Generally, while the MCC is valuable, states regard MCCs as a supplementary vehicle, not a replacement for MRBs. Since MCCs are not refundable, households that do not have tax liability--a large segment of the first time homebuyer market--cannot use them. Moreover in capital deficient states, MCCs do nothing to increase the flow of mortgage capital to the state.

Like MRBs, MCCs are scheduled to sunset on Dec 31, 1988. This prospect is of special concern to states in light of troubling housing trends.

Recognizing that States have had and can continue to have an impact on homeownership, states are asking Congress to extend the MRB and MCC programs beyond 1988. However, these vehicles, in and of themselves, are not enough. For this reason, CSHA is especially pleased that these hearings are being held. Expanding opportunities for homeownership should be a national policy objective. Its successful realization is stymied by the affordability problem facing the nation.

Today, states acknowledge it will take national, state, and local efforts to reverse the homeownership trends of recent years. We can look back at a history of housing policy concentrated primarily along a federal-local axis. This is changing. As the testimony of the state housing finance agencies indicates, innovative and imaginative means are being devised for dealing with the affordability problem which is limiting homeownership opportunities. In many cases, state and agency resources are being directly employed. We have attached three recent publications, entitled:

--Housing Initiatives of State Housing Finance Agencies, (CSHA, 1987),
--Production Activities of State Housing Finance Agencies/ 1985 and Cumulative, (CSHA, 1986), and,
--State Initiatives in Elderly Housing, (CSHA, 1986).

These publications detail the expanding state HFA activities and programs we have been discussing.

Realistically, though, state resources for use in housing are not plentiful and vary among states, in some cases radically. The presence of the federal government is essential. If homeownership opportunities are to once again expand, states housing finance agencies can lend their experience in working within their state's housing markets, and lend the resource of expertise which is present. Clearly, state HFAs provide a stable and capable vehicle for federal support.

The Council of State Housing Agencies has initiated a policy formulation process which over the coming summer months will develop policy recommendations on homeownership and in rental housing. These policy and program recommendations will be presented to this Subcommittee this fall.